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## **APPENDIX J**

### **INFORMATION RE: JOINT VENTURES AND RELATED ENTITIES**

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**CONFIDENTIAL**

**Responses To Question XII 1-8, Related Organizations**  
**March 3, 2004, Letter From U.S. Senate Committee on Finance**  
**To The Nature Conservancy**

**XII. RELATED ORGANIZATIONS**

**OVERVIEW STATEMENT**

In 1995, The Nature Conservancy ("TNC") created the Center for Compatible Economic Development ("CCED") to be a new and distinct operating unit of TNC, to work with communities in developing new conservation tools that would develop businesses, products, and land uses that conserve ecosystems, enhance local economies and achieve community goals.

TNC's then 45 years of experience in protecting significant ecosystems confirmed that long-term conservation would succeed only with strong support from the people who live and work in these areas. Economic development is vitally important to these communities, but inappropriate development often presents serious threats to local ecosystems.

Examples of development that conserve ecosystems, generate profits and enhance quality of life were rare. Therefore, successful, locally-based, compatible development initiatives were to be fostered, and the results documented and shared, to inspire efforts in other ecosystems and communities.

CCED placed special emphasis on compatible forestry, agriculture, tourism and residential development. CCED helped plan and launch sustainable development programs like the Virginia's Eastern Shore, in Appalachia's Clinch Valley, and in South Carolina's ACE Basin. CCED worked with cattle ranchers in six major ecosystems and communities during its early years to create and enhance businesses and identify markets that reinforce environmentally responsible production.

CCED's mission furthers conservation purposes by creating new jobs, helping local entrepreneurs plan, capitalize and launch new compatible businesses, and acting as a place for teaching, as well as learning, about conservation and compatible development.

## **1. REPORT TO MANAGEMENT**

Following the report to the management for the year ending June 30, 2002, The Nature Conservancy ("TNC") took the following actions with respect to identifying related entities, monitoring the relationships with related entities, and ensuring the proper reporting of related entity financial information:

- TNC staff produced an up-to-date listing of related organizations;
- a uniform definition of a "related entity" was produced by TNC staff and reviewed by PricewaterhouseCoopers (PwC) for use in the preparation of Form 990 and for accounting determinations;
- the appropriate accounting treatment for each entity was discussed with PwC;
- TNC produced a new policy and standard operating procedure, attached as Exhibit XII la;
- Information was collected on related organizations in order to accurately prepare the FY03 Form 990; and
- TNC staff identified several entities that were considered candidates for termination:
  - Bear Mountain Lodge, Inc. (in process of termination)
  - Conservation Beef, LLC (TNC withdrew from the LLC effective February 19, 2004)
  - Sustainable Forest Resources PNG-US, LLC (in process of termination)

As you are also aware, the Board of Directors of TNC has implemented new governance and monitoring procedures. And the outside Governance Advisory Panel has issued its final report on centralized oversight, which recommendations are before TNC's Board for review.

TNC Interim Report on Governance, Policies and Procedures, March 2, 2004 and Report of the Governance Advisory Panel to the Executive Committee and the Board of Governors of TNC, March 19, 2004 are attached as Exhibit XII 1b.

## **2. CONSERVATION BEEF, LLC**

The Nature Conservancy, through its operating unit Center for Compatible Economic Development ("CCED"), formed Conservation Beef, LLC ("CBL") in partnership with Artemis Wildlife Foundation ("AWF") in 1999. On January 1, 2003, TNC was formally substituted for CCED in CBL's Operating Agreement. Until February 19, 2004, when TNC withdrew from CBL, TNC and AWF each had a 50% equity interest in CBL.

In business terms, CBL is a sales and direct-marketing organization that markets fully mature, range-fed, additive-free, healthful beef ("Conservation Beef") to the consumer and corporate gift markets and to a small number of highly visible, food-source-conscious restaurants.

CBL's mission is to conserve biologically significant lands in the western United States by developing market forces that will support economically sustainable and ecologically sound cattle ranching. CBL's means to accomplish that mission is to create a niche market for Conservation Beef that will return a premium price to ranchers who commit to long-term land conservation strategies.

Conservation Beef is produced only on western landscapes of the highest ecological value by ranchers who commit, through strategic alliances with CBL, to long-term conservation of their open lands through ecologically sound land stewardship practices, land-use planning, and conservation easements. CBL works with its rancher-suppliers to develop those stewardship standards and coordinates the work of an independent panel of scientists and ecologists who monitor and certify adherence to the standards and evaluate their beneficial impacts on ecosystem health and wildlife habitat.

CBL has had a loss in each of the last four years with negative net income as follows: 2000, \$93,409.14; 2001, \$176,162.45; 2002, \$369,473.77; and 2003, \$441,182.52.

#### **RESPONSES TO SPECIFIC QUESTIONS NOT ADDRESSED ABOVE**

2a CBL's Articles of Organization, Operating Agreement, as of October 20, 1999, First Amended and Restated Operating Agreement, as of January 1, 2003, and Agreement to Withdraw and Promissory Note, dated February 19, 2004, are attached as Exhibit XII 2a.

2b Capital contributions and profit/loss allocations are addressed in CBL's Operating Agreement, which specifies a sharing ratio of 50% for each equity owner (section 1.44) as applied to profits and losses (section 9.1). Although AWF contributed only 28% of the cash capital to CBL, the parties agreed to equal sharing ratios because AWF also contributed its relationships and contacts and staff expertise and time. Neither equity owner was required to make any additional capital contributions under the provisions of the Operating Agreement (section 8.2). Note: references are to the 2003 Restated Operating Agreement.

2c Because AWF is an independent organization, TNC does not have a copy of its determination letter.

2d Because AWF is an independent organization, TNC does not have a copy of its most recent Form 990.

2e The concept of Conservation Beef originated with William Weeks and Brian Kahn, both senior staffers of TNC, in 1995. Mr. Kahn subsequently moved to AWF, where he remained interested in the idea. TNC (through its operating unit CCED) and AWF together approached the W. Alton Jones Foundation for initial support for the project. The Foundation expressed support and recommended that TNC and AWF explicitly work together on developing the concept of Conservation Beef, with AWF contributing its connections and relationships with cattle ranchers and the time and expertise of its staff.



2f The "loss allocable to exempt purposes" of \$372,512 on CBL's Form 1065 for 2000 was erroneously included as a line item in Statement 2. That number actually represents the total of deductions listed in lines 9-18 plus the other deductions listed in Statement 2 (exclusive of the erroneous line item for "loss allocable to exempt purposes"). Despite that error, the correct amount of loss was entered in Schedules M-1 and M-2 and the correct allocations were made on each of the members' Schedule K-1.

2g CBL's 2003 Form 1065 and 2000-2003 Financial Statements are attached as Exhibit XII 2g. TNC was unable to locate a Financial Statement for 1999, although the opening (negative) equity balance from 1999 is included on the 2000 Balance Sheet.

2h All employees of CBL are eligible to participate in the retirement plan. For the 2000 fiscal year, CBL had three employees, only one of whom was full time. For the 2002 fiscal year it had four, three of whom were full time; hence the increase in plan contributions.

2i AWF provided the \$40,000 loan to CBL in 2002. TNC was neither a lender nor a guarantor with respect to this loan.

2j CBL's activities further TNC's exempt land conservation purposes by promoting sustainable land use while providing western ranch operators with financial reward for good stewardship. Such rewards, in turn, help economically sustain responsible operators and thus encourage further sound land stewardship for large blocks of both publicly and privately owned land in critical areas of the western United States.

2k, ii Form of Joint Venture Agreement with PM Holdings, LLC; PM-Conservation Beef Protocol for Live Animal Handling, Harvest, Beef Fabrication, Portioning and Shipping; Conservation Beef Option/Purchase Agreement with John Crumley (missing last 2 pages); Conservation Beef Option/Purchase Agreement with Karl Ohs, dated May 5, 2000; Conservation Beef Option/Purchase Agreement with Sun Ranch, LLC, dated September 18, 2000; Conservation Beef Purchase Agreement with John Crumley, dated September 10, 2001; Conservation Beef Purchase Agreement with Sun Ranch, LLC, dated October 15, 2001, are attached as Exhibit XII 2k,ii. Financial Statements are attached as Exhibit XII 2g.

2k, iii For the fiscal years ending June 30, 1999 through June 30, 2001, TNC reported its contributions to CBL on the Form 990 as grants and allocations (Part II, line 22). Effective for the June 30, 2002 Form 990, prior contributions to CBL were reclassified as investments and the losses allocable to TNC were reported in the Form 990 as a component of gain or loss from sales of assets other than inventory (Part I, line 8). Based on consultation with our present auditors, PricewaterhouseCoopers, we will report any income or loss amount reported on the 2003 K-1 from CBL, consistent with the characterization of the amount on CBL's Form 1065.

### 3. NATURESERVE

NatureServe (see [www.NatureServe.org](http://www.NatureServe.org)) is an independent nonprofit conservation organization that provides the scientific information and tools needed to help guide effective biodiversity conservation action. NatureServe and its network of Natural Heritage programs are the leading source for information in the United States about rare and endangered species and threatened ecosystems. NatureServe was originally organized in the 1980s under the name the Association of Biodiversity Information ("ABI").

NatureServe has no structural or legal relationship with The Nature Conservancy ("TNC") other than through a Comprehensive Strategic Agreement that was entered into between TNC and ABI.

TNC has had a longstanding involvement in the creation and ongoing activities of NatureServe. Beginning in the 1970s, TNC worked to encourage the creation of Natural Heritage programs and Conservation Data Centres in each of the states in the US, in the Canadian provinces, and in several countries in Latin America. These programs worked with TNC to engage in a number of activities critical to biodiversity conservation including:

- establishing scientific standards for biological inventory and biodiversity data management;
- developing comprehensive and current databases on at-risk species and ecological communities;
- designing advanced biodiversity data management systems in partnership with information technology leaders;
- making biodiversity information available to the public through websites, publications, and custom services to clients and partners; and
- providing information products and conservation services to guide natural resource decision-making.

Today, there are 74 independent Heritage programs and Conservation Data Centres. They are typically housed in and funded by state or provincial governments. These programs also work closely with many federal government agencies. NatureServe both represents the international network of biological inventories and provides critical services to the network such as developing standards for data classification and managing data exchanges and compilations that are critical to the functioning of the network. NatureServe and the associated network not only collect and manage detailed local information on plants, animals, and ecosystems, but develop information products, data management tools, and conservation services to help meet local, national, and global conservation needs. The objective scientific information about species and ecosystems developed by NatureServe is used by all sectors of society—conservation groups, government agencies, corporations, academia, and the public—to make informed decisions about managing our natural resources. NatureServe is governed by a Board made up of prominent scientists, representatives of State Heritage Programs, and independent philanthropists. TNC's Director of External Affairs is a member of the Board of NatureServe.

TNC's substantial financial support for NatureServe is driven by our belief that NatureServe and its associated network of Heritage programs and Conservation Data Centres are critical to our mission: the conservation of biodiversity. During the formative years of the Network, TNC financed and undertook all of the activities currently performed by NatureServe. Many of TNC's central scientific staff were devoted to the support of the Heritage Network and its data have been critical in setting TNC's conservation priorities as well as the conservation priorities of many other public and private organizations. In 1999, TNC and the Heritage Network together decided that the Network would be more successful if its central functions were housed in an independent organization rather than in TNC. Because of the Heritage Network's importance to TNC's mission, TNC agreed to continue to provide funding at a level that would ensure the continuance of the bulk of the central activities of the Network (formally housed in TNC but now housed in NatureServe) for several years in order to help the new organization be successful. In return, NatureServe agreed to continue to provide TNC with access to its biological data, which is central to our conservation planning.

#### **RESPONSES TO SPECIFIC QUESTIONS NOT ADDRESSED ABOVE AND EXHIBITS**

3a Comprehensive Agreement between TNC and ABI, dated July 1, 1999, is attached as Exhibit XII 3a.

3b Because ABI/NatureServe is an independent organization, TNC does not have copies of its governing instruments and organizational documents.

3c Because ABI/NatureServe is an independent organization, TNC does not have a copy of its determination letter.

3d TNC does not receive any fee income from ABI/NatureServe. All payments under the comprehensive agreement are from TNC to NatureServe. TNC does receive interest income from a loan to NatureServe (see response to Question XII 3e below), and modest amounts of rental income and office cost reimbursements. It should also be noted that interest and rental income are excluded from unrelated trade or business income under section 512(b)(1) and (b)(3) of the Internal Revenue Code of 1986.

3e Line of Credit Agreement between TNC and ABI is attached as Exhibit XII 3e.

3f As explained in the overview discussed above, ABI/NatureServe provides data base access to TNC and support services to Heritage Enterprise as described in the Agreement. Those services assist the Heritage Enterprise and TNC to carry out its programs in preserving biodiversity. Promoting a natural heritage program through collecting data on the distributions of species in endangered ecosystems of conservation concern is consistent with and furthers TNC's mission and programs.

3g As indicated in the discussion in response to the questions discussed above, payments to Nature Serve from TNC are in accordance with the Comprehensive agreement. The differences in the level of payments for years 1999, 2000 and 2001 are due to the timing of the payments and through mutual agreements to accelerate certain cost payments for new "software" or other services. The agreement was not formally amended for these changes and the total amount to be paid by TNC to Nature Serve remains the same.

3h Because NatureServe is an independent organization, TNC is not in a position to comment on why NatureServe responded as it did on its information return Form 990.

3i Because NatureServe is an independent organization, TNC is not in a position to comment on the independent contractors listed on Schedule A to NatureServe's Form 990.

3j Because NatureServe is an independent organization, TNC is not in a position to comment on the increase in NatureServe's employees from 1999 to 2000.

3k Because NatureServe is an independent organization, TNC is not in a position to comment on the database service fees listed on Nature/Serve's Forms 990 for 2000 and 2001.

3l Because NatureServe is an independent organization, TNC does not have a copy of its financial statements for 2002.

#### **4. EASTERN SHORE ENTERPRISES, LLC**

Eastern Shore Enterprises, LLC ("ESE"), a limited liability company, was established in 1999 following the dissolution of Virginia Eastern Shore Sustainable Development Corporation ("VESC") (see below) to operate one of VESC's remnant business lines: the development and marketing of Hayman Potato Chips. The shareholders of VESC were given the opportunity to exchange their shares in VESC for interests in the newly created ESE. The interests were ultimately apportioned as follows: Suzanne Wescoat received 1%; Franey, Parr and Meha, 3%; Sun Trust Bank, 5%; and The Nature Conservancy ("TNC"), 91%. These capital and profit and loss percentages remained the same as reflected in all subsequent tax returns. TNC was the only member to make additional contributions.

The Operating Agreement of ESE, entered on October 15, 1999, and the four letter agreements concerning the exchange of shares of VESC for interests in ESE are attached as Exhibit XII 4c.

TNC has determined, after consultation with our accountants, that we do not have any corrected information with regard to ESE's 1999 tax filings.

With respect to the reported schedule of other deductions in years 2001 and 2002 in Question XII 4e, we believe that they are primarily comprised of the operating costs of ESE which were the ordinary and necessary administrative costs of operating the company including

bookkeeping, filing of tax returns, marketing, and other expenses. See Form 1065 Supporting Schedules for 2001 and 2002, which are attached as Exhibit XII 4e.

## **5. VIRGINIA EASTERN SHORE SUSTAINABLE DEVELOPMENT CORPORATION**

### **OVERVIEW OF VESC**

The Nature Conservancy ("TNC") has been working since 1969 to protect the Virginia Eastern Shore's globally significant resources. TNC's 45,000 acre Virginia Coast Reserve encompasses 14 barrier islands, pristine coastal wetlands and mainland farms, has been designated by the United Nations as a Biosphere Reserve. While the Eastern Shore is rich in natural and cultural resources, it has poor economic conditions raising the threat of incompatible development that over time could destroy rather than protect the environment. TNC worked with local community partners through its Center for Compatible Economic Development ("CCED") to develop a strategic plan for compatible economic development on the Eastern Shore. In 1995, the Virginia Eastern Shore Sustainable Development Corporation ("VESC") was created to: (1) develop and support products, and land uses that enhanced the local economy; (2) design and develop compatible businesses and promote compatible land uses that sought to reduce key stresses or potential stresses to Virginia Eastern Shores ecological systems, such as pollution of coastal waters that could lead to deterioration of the Virginia Eastern Shore; and (3) provide a healthy, sustainable economic base that obviated environmental threats and promoted opportunities for business development and job opportunities for low income individuals.

TNC, through its CCED, established the for-profit corporation VESC, financed with \$2.5 million of equity and debt capitalization from eleven institutional and individual investors. VESC, with the assistance of TNC, assembled a distinguished Board of Directors that included leaders from various public and private sector organizations.

### **VESC'S MISSION AND STRUCTURE**

When VESC was created, there were few sustainable development projects in the United States and abroad, and there was no working example of a successful sustainable development program. VESC was to be a permanent organization to implement sustainable development at the local ecosystem and community level. VESC established three operating entities: (1) Eastern Shore Products, to develop, license, and market a range of products intended to focus initially on compatible nature-based tourism, especially agricultural products sustainably produced on seaside farms and local crafts and other products that would provide businesses and job opportunities for low income citizens; (2) Eastern Shore Venture Fund, to provide loans and capital to new and existing business enterprises that employed ecologically compatible and economically sound development practices but could not secure financing from conventional sources; and (3) Eastern Shore Lands, to serve as a vehicle to implement

sustainable development of the landscape through the acquisition, lease and resale of seaside farm and village properties with conservation plans and restrictions.

During its early start-up period, many of its initial plans were tested and revised. The VESC Business Plan had called for the farming of organically grown produce. Few farmers were interested, however, in making this commitment to convert to organic farming. Rather there was some interest in selling the indigenous Hayman potato locally grown for generations but never aggressively marketed off the Eastern Shore. Local artists and crafts people resisted moving toward the required large production volumes that were necessary to bring in arts and crafts businesses on a financially sustainable scale. Eastern Shore Venture Fund was faced with low levels of entrepreneurial activity which produced limited opportunities for the proposed Venture Fund. Eastern Shore Lands planned to develop compatible residential development and related products. However, these activities were not pursued and delays in marshalling a constituency for a nature-based tourism lodging facility prompted the corporation to reconsider and to begin marketing nature-based programs. After reevaluation of the business plan programs, the VESC decided to concentrate on test marketing the Hayman Potato and Hayman Potato Chip project and establish a list of weekend tourism package called Eastern Shore Escapes. In 1999, CCED reassessed VESC's viability and ultimately the program was dissolved.

#### **RESPONSES TO SPECIFIC QUESTIONS NOT ADDRESSED ABOVE AND EXHIBITS**

5a List of VESC's investors and lenders is attached as Exhibit XII 5a.

5b VESC's Articles of Incorporation; Bylaws; Register of Shares of Stock Issued and Outstanding and Individual Shareholders Record of Shareholdings; and Subscription Agreements with TNC, Mary Eyre Peacock, Crestar Financial Corporation, Virginia Environmental Endowment, and Allen & Company, and other documents regarding share transfers are attached as Exhibit XII 5d.

5c See Exhibit XII 5a.

5d Loan documents for loans from the Ford Foundation, Mary Flagler Cary Charitable Trust, and Lincoln-Lane Foundation are attached as Exhibit XII 5d.

Our understanding of the loans are as follows:

(1) Note payable to the Ford Foundation in the amount of \$1,000,000. During 1995, VESC borrowed a principal sum of \$500,000 from the Foundation. The principal sum was payable in two annual installments of \$150,000 each due on December 1, 2001 and December 1, 2002 and one annual installment of \$200,000 due on December 1, 2003. The interest rate was 2% per annum and is payable on a quarterly basis. The note agreement requires VESC to maintain a current ratio of at least 1.25 and net worth as a percentage of total assets of at least 35%. In addition, distributions to shareholders were not

allowed prior to December 1, 2000, and, in certain circumstances, limited thereafter. VESC was not in compliance with the net worth covenant at December 31, 1998. As a result, this note was callable at the option of the Ford Foundation and was classified as a current liability on VESC's Financial Statement.

(2) Note payable to Mary Flagler Cary Charitable Trust for \$400,000. The entire principal amount outstanding was convertible at the holder's option into Class A Voting Common Stock of VESC at a price between \$1,030 and \$1,150 per share on June 1 of the years 1996 - 2000. If the holder does not exercise the Optional Conversion, the principal amount was payable in 19 consecutive and equal quarterly installments of \$10,000 commencing on September 1, 2000. The maturity date is June 1, 2005. This note did not bear interest until June 1, 2000, at which time interest shall accrue on a quarterly basis at the rate equal to the 3-months' London Interbank Offered Rate.

(3) Note payable to Lincoln-Lane Foundation of \$100,000. The entire outstanding amount was convertible at the holder's option (Optional Conversion) into Class A Voting Common Stock of VESC at \$1,275 per share on December 1, 2000. If the holder does not exercise the Option Conversion, the principal amount of this note shall be payable in 11 consecutive and equal quarterly installments of \$8,333 commencing on March 1, 2001. The maturity date is December 3, 2003. The interest rate is 3% per annum and is payable on a quarterly basis.

On liquidation of VESC, the amounts owed on notes payable were: Ford Foundation, \$106,000; Mary Flagler Carey Charitable Trust, \$84,800; and Lincoln Lane Foundation, \$219,592.

5e To the best of our knowledge and belief, VESC entered into no royalty agreements. It is possible that royalty expenses were paid incident to payments related to the work of local artisans.

5f Copies of VESC's Form 1120 for 1996 through 1997 are attached as Exhibit XII 5f. TNC was unable to locate VESC's Form 1120 for 1995. Instead, VESC's Financial Statements for the four months ended December 31, 1995 are also attached as Exhibit XII 5f.

5g Promissory Note from TNC to VESC, dated December 1, 1998, and accompanying payment ledger; and Promissory Note from TNC to VESC, dated May 20, 1999, and accompanying payment ledger are attached as Exhibit XII 5g.

5h Waterside Capital Corporation is a federally chartered Small Business Investment Company based in Hampton Roads, Virginia, which made loans to qualified small businesses on the Eastern Shore. VESC invested \$50,000 in Waterside Capital in lieu of establishing the "Eastern Shore Venture Fund" that was to provide loans and investment capital to new and existing enterprises which met certain criteria for ecologically compatible and economically

sound development. Later, after the investment had been made in Waterside Capital, Alan Lindauer, its President and CEO, joined the VESC Board of Directors.

5i See Exhibit XII 5a.

5j The debt was held by the Ford Foundation, the Mary Flagler Cary Trust, and Lincoln Lane Foundation. See response to Question XII 5d above.

VESC entered into a series of negotiations with its debt holders. In a memorandum dated May 26, 1998, the Ford Foundation agreed to a waiver of the default provisions under certain circumstances because of VESC's impending failure to meet certain loan requirements. As a result, CCED agreed to engage an independent group of experts to conduct a strategic review and evaluation of VESC. Using this strategic review, VESC would update and revise its business strategy and financial projections and a proposed "downside plan" for the next two years for those assumptions in the business plan that were not borne out. The Ford Foundation would then make the second installment of \$500,000 under certain conditions: the \$500,000 full recourse loan would be made to TNC rather than VESC and TNC would invest the \$500,000 in VESC with the approval of the TNC Board.

The Final Report of the Assessment of VESC was prepared by the independent advisory group on December 7, 1998. The report found that VESC required ongoing capital infusions and concluded that the trends did not support VESC's March 1998 Financial Pro Forma Projection that the Company would be operated on a break even basis. The report considered four options for VESC:

- recapitalization;
- liquidation;
- assignment or sale of separate business lines; or
- acquisition of VESC trademarks accounts, product lines, and customer lists by a for-profit company.

After reviewing the preliminary findings, TNC and VESC decided to recapitalize a scaled-back VESC.

Following the issuance of this report, VESC, on February 17, 1999, contacted Ford Foundation to formally request a modification of the terms of the initial loan agreement of December 1, 1995. Under that loan agreement, Section 6.8.1, VESC was required by December 31, 1997 to establish that its net worth as a percentage of total assets was not less than 35%. When VESC advised Ford that it had failed to meet the target percentage, a request was made to extend the period of time required to meet the percentage. Ford agreed to a one time extension to September 30, 1998 to waive the Event of Default clause by violation of section 6.8.1 of the loan agreement. Subsequent to September 30, 1998, VESC was not able to show that it met the terms of section 6.8.1 of the loan agreement. In a letter dated May 3, 1999, the Ford Foundation project manager, Jeffrey T. Olson, advised TNC that he had recommended that the Foundation make no further grants to The Nature Conservancy and that VESC was in default under the loan agreement causing the balance of the note plus interest



accrued to become immediately due and payable unless a satisfactory proposal to remedy the default was submitted within the next few weeks. On June 3, 1999, in preparation for a final decision meeting with Ford Foundation on June 8, VESC submitted a five-year financial projection, financial statements as of April 1999, and newly conducted audit by Goodman and Company, LLP of Norfolk. On June 8, 1999, Ford Foundation did not approve payment of the second \$500,000 installment.

5k No real estate investments were made, although the VESC Business Plan had originally provided for Eastern Shore Lands Project to serve as a vehicle to lease and resell seaside farms. That program was never initiated or pursued by VESC. VESC, however, did hold one property, MillCreek Farm, which was transferred to VESC by TNC as an initial capital investment, valued at \$500,000. In 1998, VESC still owned a 60% interest in the property.

5l See the Chart in Exhibit XII 5a listing the Class A and B stockholders. VESC was authorized to issue 2,000 shares of Class A voting common stock, no par value, 500 shares of Class B voting common, no par value stock. VESC's Articles of Incorporation, Section B, provided for the shareholder rights on the distribution of dividends and other preferences. Class B shareholders elected the majority of the Board but were subordinate to Class A shareholders on liquidation.

5m TNC, through CCED, established VESC. See "Overview of VESC" above and response to Question XII 5l.

5n VESC Board Minutes of August 3, 1999 regarding the orderly dissolution of the company, and Unanimous Consent of Shareholders to Dissolve Corporation, effective as of October 26, 1999, are attached as Exhibit XII 5n.

## **6. ADIRONDACK LAND TRUST**

The Nature Conservancy ("TNC") and the Adirondack Land Trust ("ALT") entered into a memorandum of understanding to promote mutual goals of protecting the land and water resources of the Adirondack-North Country region. TNC continues to be involved in this program. Under this relationship, TNC provides administrative services to ALT.

6a Memorandum of Understanding, dated October 3, 1988, and the successor Contractual Agreement, effective February 23, 2004, are attached as Exhibit XII 6a.

6b As indicated in the agreements attached in Exhibit XII 6a, TNC staff provides services to the ALT as a matter of economic efficiency.

## **7. STM/TNC LLC**

STM/TNC LLC ("STM") was formed in 1993 to facilitate the program-related investments of the Summner T. McKnight Foundation (the "Foundation") to protect the fragile ecosystem and historic way of life of the watermen at Willis Warf on the Virginia Eastern Shore. In furtherance of those goals, STM has owned three parcels of land at Willis Wharf and offers bare ground leases for appropriate tenants and thus seeks to promote development of the waterfront in a sustainable and ecologically sensitive manner, while promoting the economic well-being of the local community, including by the establishment of a Willis Wharf Waterfront Center to include waterfront facilities, a visitors' center, stores, restaurants, a marine research center, and improved water access for both fishermen and other community members. STM has sold one of the properties but continues to hold the other two.

The only relationship between the Foundation and TNC is the joint ownership of STM. TNC's ownership of STM and partnership with the Foundation furthers TNC's long-term goal of protecting the Virginia Eastern Shore's globally significant resources by acting in concert with other local community partners in encouraging compatible economic development on the Virginia Eastern Shore.

There was no formal relationship between STM and Virginia Eastern Shore Sustainable Development Corporation ("VESC"). They had mutually shared goals of conservation and economic development on the Virginia Eastern Shore and STM thus called upon VESC to assist it in preparation of model development options that were to be a part of STM's Business Plan.

## **8. THE FOREST BANK LLC**

The Nature Conservancy formed The Forest Bank, LLC ("TFBL") as a Delaware limited liability company in January of 2001. TFBL's goal was to acquire from owners of forest land the rights to maintain, conserve, selectively cut, manage, sell, retain the proceeds from, and regenerate the trees located on each owner's property in exchange for units of membership interest in TFBL. TFBL's membership units would have entitled the holders to preferred annual distributions based on the value of the timber rights contributed to TFBL.

TFBL had two primary objectives. First, it sought to conserve the forests, lands, and watersheds of the regions in which it was to acquire timber rights. Second, it sought to maximize the sustainable financial return to the members who contributed timber rights to it. TFBL's limited liability company agreement expressly required, however, that if there were a conflict between the forest conservation objectives on one hand and any of the economic objectives on the other hand, TFBL's forest conservation objectives were to take priority.

Despite a public offering of its membership units, TFBL was unable to attract any investors to its novel concept and so was dissolved on November 6, 2002.

## **RESPONSES TO SPECIFIC QUESTIONS NOT ADDRESSED ABOVE**

8a Certificate of Cancellation of TFBL is attached as Exhibit XII 8a.

8b TFBL's SEC filings are provided in separate binders as Exhibit XII 8b.

8c TFBL's Certificate of Formation and Amended and Restated Limited Liability Company Agreement are attached as Exhibit XII 8c.

8d The subscription process and a summary of what the subscription agreement would entail are described in TFBL's Form S-1. No subscription agreements were ever executed. TFBL's Form of Subscription and Contribution Agreement is attached as Exhibit XII 8d.

8f TFBL was liquidated because it was unable to attract any investors and therefore had no capital with which to conduct its operations.

8g TFBL's legal expenses pertain primarily to the review and preparation of the public registration materials for the offering of securities.


8h TNC anticipated selling ownership interests in TFBL and therefore would not remain the sole owner of TFBL. As was noted in the response to Question 8f above, no securities were sold and TFBL was dissolved. For federal tax purposes, TFBL was treated as a partnership under the assumption that any tax effects from the operation of TFBL would be shared by its multiple owners. The U.S. Federal Income Tax Opinion provided by Hunton & Williams in draft form is attached as Exhibit XII 8h.

**Exhibits Accompanying Responses to  
Question XII 1-8  
Related Organizations  
March 3, 2004, Letter  
From U.S. Senate Committee On Finance  
To The Nature Conservancy**

**Tabs**

1. Exhibit XII 1a TNC Policy and Standard Operating Procedure
2. Exhibit XII 1b Governance Advisory Panel Reports
3. Exhibit XII 2a CBL Organizational Documents
4. Exhibit XII 2g CBL 2003 Tax Return and 2000-2003 Financial Statements
5. Exhibit XII 2k,ii CBL Contracts
6. Exhibit XII 3a Comprehensive Agreement
7. Exhibit XII 3e Line of Credit Agreement
8. Exhibit XII 4c ESE Operating Agreement and Exchange Letter Agreements
9. Exhibit XII 4e ESE Form 1065 Supporting Schedules
10. Exhibit XII 5a VESC Lists of Investors and Lenders
11. Exhibit XII 5b VESC Organizational Documents and Share Subscription Documents
12. Exhibit XII 5d VESC Loan Documents
13. Exhibit XII 5f VESC Forms 1120 for 1996-1997 and Financial Statements for 1995
14. Exhibit XII 5g VESC Promissory Notes
15. Exhibit XII 5j VESC Form 1120 for 1999
16. Exhibit XII 5n VESC Liquidation Documents
17. Exhibit XII 6a Memorandum of Understanding and Contractual Agreement
18. Exhibit XII 8a TFBL Certificate of Cancellation
19. Exhibit XII 8c TFBL Organizational Documents
20. Exhibit XII 8d TFBL Form of Subscription Agreement
21. Exhibit XII 8h TFBL Form of Tax Opinion

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# Finance

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## Policies

### Standard Operating Procedure

## Related Entities

### POLICY:

#### Definitions

Related entities, as the term is used herein, refers to the following categories of relationship:

- Wholly-owned Conservancy Not-for-Profit Corporations - incorporated as legal entities, but conducting no substantive operations; generally necessary to hold title/do business in a given state/country;
- Controlled Not-for-Profit Organizations - through majority board membership or other form of controlling financial interest;
- Owned or Controlled For-profit Entities - through majority stock ownership or majority LLC ownership;
- Partnerships/Joint Ventures - relationships established by formal legal agreements with others where the Conservancy is a named partner in an ongoing conservation or business operation and has a greater than 50% interest in the venture;
- Trusts - separately created entities where the Conservancy is a trustee or acts in a similar management capacity, but is not merely a beneficiary (excludes, for example, planned giving trust arrangements and the like); and
- Other - arrangements where the Conservancy acts as financial fiduciary or agent for other organizations, coalitions, etc., who are using our Tax Identification Number or are otherwise conducting their activities under the duly authorized auspices of The Nature Conservancy.

#### Acquisition/Creation of Related Entities

Relationships with any entities falling within any of the above categories that result from the receipt of a gift to the Conservancy, the purchase of an interest in an entity by the Conservancy, or the creation of a new entity by the Conservancy must be approved by the Board of Governors prior to the acceptance/purchase/creation of the entity. Considerations for approval include, but are not limited to: 1) consistency with the Conservancy's mission, strategy and values; 2) need for a separate legal entity; 3) additional risks/costs; and 4) tax/reporting implications. Exceptions to the requirement for Board approval may be made by the President or Chief Financial Officer when interests in entities are contributed by gift solely to enable the Conservancy to acquire and sell the underlying assets for fundraising purposes.

Actions taken by the Conservancy to acquire/create any new related entity must be reported to the Worldwide Office Legal Function and Worldwide Office Finance Function at the time of acquisition/creation to ensure proper inclusion in the Conservancy's corporate records and financial reports. Original documentation relating to the acquisition/creation of related entities (e.g. articles of

incorporation, by-laws, partnership agreements, trust documents, etc...) should be provided to, and maintained by, the Worldwide Office Legal Function. Copies should be sent to Worldwide Office Finance Function and maintained in files of the responsible Operating Unit (i.e. State, Country, Division, Region, or Worldwide Office Function).

#### Ongoing Responsibilities

Once the relationship is established, organizational responsibility for governance, oversight, filing of required reports (audited financial statements, tax returns, etc.) and other administrative actions necessary to fulfill the Conservancy's responsibilities in the relationship rest with the Operating Unit responsible for the acquisition/creation of the related entity. Annual financial statements and any other documentation necessary to meet the Conservancy's corporate filing responsibilities shall be provided to the Worldwide Office Finance Function within 90 days of the close of the fiscal year of the related entity. If full financial statements, with footnotes, are not prepared, notification of significant transactions between the related entity and the Conservancy must be reported to Worldwide Office Finance Function in addition to any other financial information provided.

A current listing of related entities will be maintained by Worldwide Office Finance Function on the Conservancy Intranet. The list will be validated by Worldwide Office Finance Function personnel annually in conjunction with the preparation and filing of the Conservancy's informational return - IRS Form 990.

#### PURPOSE:

Approval of new business relationships is necessary to ensure that all activities are consistent with Conservancy strategy and that related risks are identified and managed.


#### ORIGIN:

New, as Policy. Revision of former Standard Operating Procedure entitled "Controlled Corporations, Partnerships or Joint Ventures." Approved by the Board of Governors January 30, 2004.

#### REFERENCES, RESOURCES and EXPLANATORY NOTES:

Guidance relating to the reporting of related entities by Not-for-Profit Organizations is provided by American Institutes of Certified Public Accountants' Statement of Position 94-3. A full reading of the document is encouraged. For purposes of this policy, circumstances where the Conservancy is required to, or has the option to, consolidate the activities of another not-for-profit organization define it as a related entity. Beyond majority voting control, this includes situations where the Conservancy controls another not-for-profit entity through a combination of less than majority voting and an economic interest. Control is defined as the direct or indirect ability to determine the direction of management and policies through ownership, contract, or otherwise.

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## Policies

### Standard Operating Procedure

## Significant Business Interests in Separate Legal Entities

### STANDARD OPERATING PROCEDURE:

#### Application

This standard operating procedure applies to any transaction that involves the Conservancy's acquisition of a significant business interest in a separate legal entity that does not constitute a controlling interest in such entity but that does constitute more than a purely passive investment. For purposes of this standard operating procedure:

1. A "separate legal entity" includes any for-profit corporation, nonprofit corporation or nonprofit organization, general partnership or limited partnership, limited liability company, joint venture or other comparable organization or entity.
2. A "significant business interest" is:
  - a. Any ownership interest in a separate legal entity that (i) has a fair market value in excess of \$100,000 and (ii) is more than a purely passive investment in the separate legal entity but is not a controlling interest in the separate legal entity. The fair market value of the Conservancy's ownership interest shall be determined at the time the ownership interest is acquired, whether by purchase or by gift. If ownership interests in the same separate legal entity are acquired over time, then the fair market value of the entire ownership interest that will be owned by the Conservancy as the result of each acquisition will be determined. If such cumulative value exceeds \$100,000, the ownership interest is then a "significant business interest."
  - OR
  - b. Any management, voting or other decision-making right or interest in a separate legal entity which involves an investment on the part of the Conservancy in excess of \$100,000 (or value equivalent), whether initially or cumulatively over time. Examples of such management, voting or other decision-making interests include: (i) the Conservancy's right to appoint a director, trustee or other member to the entity's

governing body or executive or management committee (but not including an advisory committee) or to exercise voting rights on entity management matters (including voting rights to elect the entity's executive officers) and (ii) service of a Conservancy Board member or officer as a member of the governing body of the separate legal entity.

For guidance regarding the Conservancy's creation or acquisition of a controlling ownership or controlling management interest in a separate legal entity, reference should be made to the Conservancy's policy entitled "Related Entities."

#### Approvals and Notifications

Any transaction involving the Conservancy's acquisition of a significant business interest in a separate legal entity must be approved by the President prior to such acquisition. Approval of the Conservancy's acquisition of a significant business interest in a separate legal entity will be based on an evaluation of the following factors: (1) consistency with the Conservancy's mission, strategy and values; (2) the financial, legal and other risks and costs; (3) the tax and other legal and financial reporting implications; and (4) public perception. An exception to the requirement for Presidential approval may be made by the Chief Financial Officer when the Conservancy acquires a significant business interest in a separate legal entity as a gift with the sole intention of promptly re-selling such significant business interest for fundraising purposes. In any case, the President and Chief Financial Officer should apprise the Board of Governors of any acquisition of a significant business interest in a separate legal entity that poses significant financial, legal or other risks to the Conservancy. Once approved, the Conservancy's acquisition, and subsequent handling, of a significant business interest in a separate legal entity should be reviewed and approved by a Conservancy attorney.

#### Responsibilities

The Conservancy staff directly responsible for carrying through with the Conservancy's acquisition of a significant business interest in a separate legal entity which has received the required approvals must report all actions relating to such acquisition to the Worldwide Office Finance Department and provide to the Worldwide Office Finance Department copies of relevant documentation evidencing such significant business interest. All original documentation relating to the Conservancy's initial acquisition and subsequent holding or handling of such significant business interest should be maintained by the Worldwide Office Legal Function. Once the Conservancy has acquired a significant business interest in a separate legal entity, the Operating Unit or Worldwide Office function responsible for the Conservancy's acquisition of such significant business interest will (1) be responsible for fulfilling all of the Conservancy's legal, tax and reporting obligations relating to such significant business interest, and (2) use its best efforts to obtain the annual financial information for such separate legal entity as soon as reasonably possible following the fiscal year end of such entity and promptly provide a copy of same to the Worldwide Office Finance Department in order to ensure proper recording of such significant business interest in the Conservancy's financial records.



**PURPOSE:**

Approval of the Conservancy's acquisition of any significant business interest in a separate legal entity is necessary to ensure that all activities are consistent with the Conservancy's strategy and that related risks are identified and managed. Reporting financial information in a timely manner helps to ensure proper recording in the Conservancy's financial records.

**ORIGIN:**


Established February 2004, recommended by the Audit Committee of the Board of Governors as a companion to the policy entitled "Related Entities."

**REFERENCES, RESOURCES AND EXPLANATORY NOTES:**

Refer to policies entitled "Related Entities" and "Conflict of Interest," and to standard operating procedure entitled "Non-Real Estate Contracts."

**RESPONSIBLE FUNCTION/PARTY:**

Worldwide Office Finance Function

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Last Updated On 03/04/2004

March 2, 2004

**The Nature Conservancy  
Interim Report on Governance, Policies and Procedures**

The mission of The Nature Conservancy is to preserve the animals, plants and natural communities representing the diversity of life on Earth by protecting the lands and waters they need to survive. This mission is pursued through a science-based planning process ("Conservation by Design"), which enables the Conservancy to identify the highest priority places that, if conserved, promise to result in meaningful and lasting conservation results.

The Conservancy has been and remains committed to carrying out this mission in accordance with the letter and spirit of all applicable laws and the highest ethical standards. In recent years, the Conservancy has grown substantially, both in absolute size and in the number and complexity of the transactions it undertakes to carry out its conservation mission. During this same period, policymakers and others have properly focused increased attention on the governance and activities of non-profit organizations, including the Conservancy.

Recognizing the need to strengthen its organizational governance and oversight, the Conservancy's Board of Governors and staff in June 2003 launched a comprehensive review of its governance processes and its specific policies and procedures for land transactions and other activities. The principal changes resulting from this review are described below. The Conservancy is continuing with its review and will announce further changes as they are made.\*

**Governance Structure and Processes**

At the direction of the Conservancy's Board of Governors in June 2003, the Conservancy initiated a comprehensive review of its governance structure and processes. This review has resulted in four sets of changes intended to strengthen the Conservancy's ability to carry out its mission successfully while maintaining an appropriate balance between decentralized functioning (one of the Conservancy's core strengths) and centralized oversight.

1. *Restructuring of the Board of Governors.* With the assistance of an independent panel with substantial experience in governance issues, the Board of

---

\* Many of the changes described in this memorandum have previously been approved by the Conservancy's Board of Governors. Certain of the remaining changes requiring Board ratification will be presented to the Board for approval on March 12, 2004.

Governors has been restructured to enable it to assume a more active oversight role as well as define and manage the important relationship between the Conservancy and its State chapters and their trustees. To accomplish these goals, the Board of Governors created an Executive Committee that will meet frequently and revitalized its other committees, which will be directly and actively engaged in oversight and strategic decisions. The Board committees are each chaired by a non-employee member of the Board and include the following: strategy; governance; conservation project review; audit; finance; and marketing and philanthropy.

2. *Business and Reputational Risk Committee.* The Conservancy has a broad range of specific policies and procedures, but no set of policies and procedures can identify in advance all possible instances that may present financial, legal, ethical or reputational risk to an organization such as the Conservancy as a whole. Moreover, there may be instances where established policies and procedures would prohibit the accomplishment of critical conservation goals and it occasionally may be appropriate in certain specific situations to permit critical conservation goals to be accomplished in a manner consistent with the intent and purposes of the applicable policies and procedures.

To address these issues, the Conservancy has authorized creation of a Business and Reputational Risk Committee whose activities will be modeled on the committee review process increasingly used by decentralized firms, in the financial services sector and elsewhere, for risk review. The committee will conduct advance reviews of those projects and transactions that meet its criteria for review (e.g., transactions that are new, novel or particularly complex and transactions that comply with all applicable legal requirements and Conservancy policies but nevertheless involve potentially substantial financial, legal, ethical or reputational risk to the Conservancy).

The committee's members will consist of experienced Conservancy personnel representing all relevant disciplines necessary to evaluate critically the organizational risks associated with the projects and transactions it reviews. The committee will endeavor to promote intelligent and prudent entrepreneurship by helping innovative conservation projects succeed whenever feasible. Thus, the committee will have the ability not simply to approve or disapprove a proposed project or transaction as presented, but to grant approval conditioned on restructuring the project or transaction in ways that would address organizational risks effectively and ensure full compliance with all applicable laws and relevant ethical considerations.

3. *Conflicts of Interest.* The Conservancy has long had a conflicts of interest policy intended to ensure proper advance review of transactions involving employees, directors, State trustees and other related parties. This policy has been administered by the Conservancy's law department and the review process focused primarily on the potential misuse of proprietary information and ensuring that terms of all such transactions met the arm's length standards of applicable law.

The Conservancy has adopted a strengthened conflicts of interest policy. This strengthened policy has two components. First, as discussed elsewhere in this memorandum, some transactions (such as land sales to related parties) are prohibited. Second, other transactions involving related parties are permitted only following review and approval to ensure compliance with all applicable laws and relevant ethical considerations.

The strengthened conflicts of interest policy contains a series of new procedures, including the following: (a) all transactions with major donors will now be subject to review; (b) a new interdisciplinary committee of experienced Conservancy staff will supplement law department review of all potential conflicts; (c) actual or potential conflicts involving special circumstances (e.g., those with organization-wide implications and those involving members of the Conservancy's Board of Governors) will be referred by the staff committee to the Audit Committee of the Board of Governors for decision; and (d) additional guidance will be provided to Conservancy employees to enable them to identify and evaluate potential conflict situations, and seek review on a timely basis.

4. *Sarbanes-Oxley Reforms.* Although the Sarbanes-Oxley Act generally does not apply to non-profit organizations such as the Conservancy, the Board of Governors concluded that several of the principles of governance underlying that legislation should be incorporated into the Conservancy's policies and procedures.

Specifically, the Conservancy has adopted a written "*whistleblower*" policy to ensure that any employee who wishes to report a suspected violation of law may do so without fear of retaliation. In addition, the Conservancy will publish a *code of conduct* and key managers will be required to execute an *annual certification* that they have complied with the code and other applicable Conservancy policies and procedures. The Conservancy has also strengthened its *internal audit* function. Under the supervision of the *audit committee* of the Board, the internal audit staff will expand the scope of its audit program to include land transactions; managers will be required to provide written reports on the manner in which they have implemented internal audit findings and recommendations; and procedures will be implemented to identify and take appropriate remedial action with respect to internal audit findings that have systemic implications. Finally, the Board of Governors has authorized the creation of a senior level position for a *chief compliance officer* who will have organization-wide responsibilities with respect to ongoing training of all staff and establishing systems to promote compliance with all applicable laws and the highest ethical standards.

#### Specific Policies and Procedures

The Conservancy's review of its specific policies and procedures governing the structure and execution of land conservation transactions and other activities and practices of the Conservancy has resulted in numerous changes, as described below.

1. *Prohibition of Purchases and Sales of Land Involving Related Parties.* Under current tax laws, transactions between organizations such as the Conservancy and related parties are permitted so long as they are structured to satisfy arm's-length standards. Nevertheless, the Conservancy has prohibited all purchases and sales of land (including interests in land, such as easements) involving related parties. For this purpose, a "related party" means any person who, within the 12 months preceding a proposed purchase or sale, was a member of the Board of Governors, a Chapter Trustee or an employee. In addition, the prohibition applies to close relatives of any such individual and entities in which the individual and/or a close relative owns more than a five percent equity interest. (Related party transactions not involving the purchase or sale of land will be subject to enhanced scrutiny under the Conservancy's strengthened conflicts of interest policy.)

2. *Special Rules for Purchases and Sales of Land Involving Major Donors.* All purchases and sales of land (including interests in land, such as easements) involving major donors will be subject to advance scrutiny under the Conservancy's strengthened conflicts of interest policy. For this purpose, a "major donor" means any individual, corporation, foundation or other entity that has made gifts or pledges of at least \$100,000 (in cash or in kind) on a cumulative basis within the 5-year period preceding the proposed transaction.

3. *Special Rules for Conservation Buyer Transactions.* Conservation Buyer transactions involve the purchase of land by the Conservancy followed by the resale of the land to an individual or organization (other than a governmental entity or other non-profit organization) subject to conservation restrictions, typically in the form of a permanent easement, limiting the uses to which the land may be put and thus reducing its value. In some instances, the Conservancy may seek a contribution from the conservation buyer or a third party in order to offset its costs, including the costs of purchasing the property prior to the imposition of the conservation easement. Of the approximately 10,000 land transactions in which the Conservancy was involved in the last 10 years, 169 were Conservation Buyer transactions.

As noted previously, Conservation Buyer transactions may no longer be undertaken with related parties and, in the case of major donors, they may be undertaken only following advance review under the Conservancy's strengthened conflicts of interest policy. In the case of those Conservation Buyer transactions that are permitted, additional special rules and procedures are now applicable. Specifically:

(a) to ensure that there is a conservation benefit to the public, the land must fall within a priority conservation site established by Conservancy scientists (which frequently involves consultation with appropriate governmental entities and others); and the terms of the easement (and the plan to monitor compliance with those terms) must be structured to achieve the desired conservation result on a permanent basis;

(b) to provide an open and equitable purchase opportunity to all potentially interested parties, the land must be offered in a manner that allows for broad exposure and fair competition among interested buyers;

(c) to ensure that the Conservancy receives fair value for the land, the Conservancy must obtain its own independent appraisal documenting the value of the property both before and after the imposition of the conservation easement;

(d) to ensure compliance with all applicable tax law requirements, all associated gifts to the Conservancy must be explicitly documented as a legally enforceable element of the Conservation Buyer transaction and the transaction must be structured in a manner that will not relieve the buyer from responsibility for substantiating the value of the gift; and

(e) to ensure that such projects are consistent with local community standards, the Conservancy will obtain community input regarding the future uses of the land.

4. *Special Rules for Gifts of Land by Related Parties and Major Donors.* Gifts of land (including interests in land such as easements), may be accepted by the Conservancy from related parties and major donors, but only if the Conservancy receives a written certification from the appraiser retained by the related party or major donor to value the gift for tax purposes. The appraiser must certify that he/she is aware of the relationship between the related party or major donor and the Conservancy and that the relationship did not influence the appraiser's conclusion as to value. The certification must also state that the appraisal satisfies all requirements for a "qualified appraisal" issued by the Internal Revenue Service. In addition, all such transactions would be subject to advance scrutiny under the Conservancy's strengthened conflicts of interest policy.

5. *Special Rules for Conservation Easements.* Conservation easements (including those imposed as part of a Conservation Buyer transaction) are now subject to strengthened procedures requiring, among other things (a) that prospective donors be informed of the Conservancy's general policies and practices to ensure a clear understanding of mutual expectations and obligations with respect to the easement; (b) standardized decision-making on the appropriate location, terms and conditions of easements; and (c) consistent monitoring and enforcement by the Conservancy of the terms of the conservation easements to which it is a party. In addition, proposed modification to easements involving related parties or major donors will be subject to advance review and approval under the strengthened conflicts of interest procedures and, as appropriate, by the Business and Reputational Risk Committee. Finally, the Conservancy will not participate in transactions which do not conform to these special

rules (including the rules discussed below governing execution of IRS Form 8283) or which are otherwise suspect or unreasonable.

6. *Special Rules for Valuation of Gifts of Land and Easements.* All gifts of land and conservation easements (including those imposed as part of a Conservation Buyer transaction) are subject to strengthened policies governing tax valuations and the execution by the Conservancy of IRS Form 8283 (required under IRS regulations in order to acknowledge receipt of the gift of the easement by the Conservancy). Specifically, the Conservancy will execute a Form 8283 given to it by a donor only if:

(a) the Form contains all information required by applicable Internal Revenue Service procedures;

(b) the donor provides to the Conservancy a copy of the appraisal to be used by the donor to establish the tax valuations shown on the Form; and

(c) the donor provides to the Conservancy a written certification by the donor's appraiser attesting that the appraiser is (i) is State-certified, (ii) has used generally accepted appraisal standards in making the appraisal, (iii) has the requisite expertise and experience to make appraisals of conservation easements and conservation lands, (iv) is not barred from practice before the Internal Revenue Service or Treasury Department or other administrative bodies, (v) has accounted for any value enhancements to other property of the donor or parties related to the donor, (vi) if the appraisal is being made for a person who is a related party or major donor with respect to the Conservancy, the appraiser is aware of the relationship and attests that it did not influence the appraiser's valuation, and (vii) the appraisal otherwise satisfies all of the requirements for a "qualified appraisal" issued by the Internal Revenue Service.

7. *Conservation Land Sales to Governments.* The Conservancy has long had a "no net profit" policy for transfers of land or interests in land to governmental agencies for conservation purposes. This policy is intended to ensure that the Conservancy only recovers its costs upon such a transfer. Recovery of such costs is of course limited by the fact that governmental agencies may only pay fair value for the property. The strengthened policy provides more detailed rules governing the calculation of direct and indirect recoverable costs, as well as special rules governing partial sales, aggregate sales and multiple sales.

8. *Compatible Human Uses.* The Conservancy has long recognized that people are an integral part of the landscape and that a reasonable amount of human use of conservation lands must be allowed. To ensure that such uses on property owned by the Conservancy are compatible with basic conservation objectives, the Conservancy has taken the following steps:

(a) to improve its decision-making, the Conservancy will initiate, in cooperation with the United States Fish and Wildlife Service, a review of scientific studies and other literature related to compatible human use;

(b) to improve its understanding of risks and inform future decisions, the Conservancy will conduct a broad survey, based on recommendations of independent scientists, of existing uses of the Conservancy's preserves; and

(c) innovative, large scale, or untested proposed human uses will be subject to advance review by the Business and Reputational Risk Committee.

In addition, in June 2003, the Conservancy's Board of Governors adopted a policy prohibiting any new oil, gas or hard rock mineral activities on the Conservancy preserves except where required by pre-existing contracts.

9. *Legislative Advocacy.* To accomplish its conservation objectives, the Conservancy often takes positions on bond referenda and other public policy issues. The Board of Governors has clarified that the Conservancy will take public positions regarding U.S. federal, State, local or international legislation, adjudicatory or rule-making proceedings, or other policy matters only if:

(a) there is a substantial and direct impact on the Conservancy's ability to accomplish its mission; and

(b) the Conservancy's participation is essential to achieve the desired outcome of the matter in question.

To ensure continued compliance with the tax law requirement that "no substantial part" of its activities consists of attempts to influence legislation (as defined), the Conservancy has strengthened its policies to provide increased training to its employees.

10. *Loans to Employees and other Related Parties.* The Board of Governors has adopted a policy prohibiting loans of Conservancy funds to any employee or member of the Board of Governors. Eligible employees may be provided with an equity advance by an independent relocation vendor if they close on a new residence prior to selling their former residence where the new residence is acquired due to a relocation by an existing employee.

11. *Cause-Related Marketing.* The Board of Governors has adopted a policy under which all new uses of the Conservancy's name and logo by third parties must be approved by the President of the Conservancy. This responsibility cannot be delegated.



12. *Related Entities.* The Board of Governors has adopted a policy with respect to the formation and operation of related entities to ensure that their activities are consistent with the Conservancy's goals and objectives and that related risks are identified and appropriately managed.

HENRY M. PAULSON, JR.  
*Chairman of the Board*

March 29, 2004

**Statement of Henry M. Paulson, Jr., Chairman, Board of Governors:  
Receipt of Final Report from Governance Advisory Panel**

The Board of Governors of The Nature Conservancy acknowledges with gratitude the final report of the Governance Advisory Panel dated March 19, 2004. Under the outstanding leadership of Ira M. Millstein, the Panel has fulfilled its mandate to provide a set of forward-looking recommendations on key issues facing the organization in the areas of governance, risk management, transparency, and accountability.

From the outset, the Panel immersed itself in the Conservancy, spending time with not only the Board of Governors' Liaison Committee, but also with senior staff, chairs of state chapter boards and chapter trustees. We commend the Panel for its commitment to understanding the Conservancy's mission and its unique, highly decentralized organizational structure prior to developing its recommendations. We also appreciate the speed with which the Panel produced its report.

The key recommendations from the Panel include:

- Strengthen the Conservancy Board's oversight of the organization by creating a more active Executive Committee and restructuring the Board's other committees.
- Build into the organization's management and board structure the means to carefully and thoroughly assess and manage organizational and reputational risks.
- Establish clear roles and responsibilities and more uniform governance standards for the Conservancy state chapters' boards of trustees.
- Seek opportunities to promote greater transparency and disclosure to more effectively inform supporters and partners of the organization's activities and policies.

Over nine months ago, the Conservancy made an organization-wide commitment to strive for the best standards in governance in the non-profit sector. With the assistance of this esteemed Panel, and through our own comprehensive internal review of our governance structure, we have made significant progress toward that commitment.

We have implemented many of the Panel's recommendations to enhance governance, including strengthening the Board's structure, which were outlined in the Panel's interim report dated January 30, 2004. We have significantly strengthened our policies and procedures, and we are well along in the process of strengthening our risk control measures. We are pleased to note that all the actions we are currently taking are consistent with the Panel's recommendations.

Statement of Henry M. Paulson, Jr.  
March 29, 2004  
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In addition to Ira Millstein, the Board of Governors wishes to thank the entire Panel: Derek C. Bok, Claudine B. Malone, Richard T. Schlosberg III, and Thomas J. Tierney; the staff of the Conservancy; Conservancy state chapter chairs and trustees; and those outside our organization whose collaboration with the Panel resulted in this highly constructive report.

The Nature Conservancy looks forward to continuing its leadership role in conserving lands and waters around the world and in nonprofit governance and operation, employing best practices as we seek to save the last great places on Earth.

**REPORT**  
**OF THE GOVERNANCE ADVISORY PANEL**  
**TO THE**  
**EXECUTIVE COMMITTEE**  
**AND THE**  
**BOARD OF GOVERNORS**  
**OF**  
**THE NATURE CONSERVANCY**  
**MARCH 19, 2004**

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## Introduction

On June 13, 2003, following a series of stories in *The Washington Post*, the Board of Governors of The Nature Conservancy announced a number of substantive changes it would make in its programs, focusing on five areas: conservation buyer transactions; cause-related marketing partnerships; resource extraction activities on Conservancy-owned lands; loans to employees; and related-party transactions. The lengthy discussion of the June 13 changes ended with these sentences:

“... the Board decided today to enlist outside perspective and expertise to help the organization continue to strengthen its governance, transparency and accountability. In the very near future, the Board will determine the exact scope and time frame of this process and announce the participants.”

By mid-August the undersigned had agreed to serve as TNC's Governance Advisory Panel. We began our discussions and operations in late August with extensive meetings involving the current and incoming TNC Board of Governors Chairs, as well as its President, followed by extensive meetings in Arlington with TNC senior staff.

In its September 29, 2003 press release formally announcing the Panel, TNC stated its goal was to become “a recognized non-profit sector leader in the areas of governance, transparency, and accountability” and that it hoped “the Panel's recommendations will be of great value to the Conservancy specifically, and the non-profit sector more broadly.”

A paper -- “Work of Outside Advisors on Key Issues” -- prepared by the Board of Governors for the Panel asked it to make a preliminary report to the Board at its January 2004 meeting, followed by the Panel's final report in March 2004 which would make detailed recommendations on governance, transparency, and accountability. The paper is annexed to this Report as Appendix A.

A Board Liaison Committee was appointed, consisting of Roger Milliken, Jr., John P. Morgridge, Admiral Joseph W. Prueher, John P. Sall, and Christine M. Scott, who served along with then-Chair Anthony P. Grassi, the incoming Chair, Carol E. Dinkins, and Henry M. Paulson, Jr., who was later elected Chair after Ms. Dinkins resigned for reasons of health. The Panel and the Board Liaison Committee met on September 24, followed by a session with the senior staff of TNC at its Arlington headquarters on September 25.

Following the Arlington meeting, the Panelists began a series of meetings and interviews, as well as frequent telephonic discussions. Beginning on November 5 and ending just prior to the Panel's meeting with the Board of Governors on January 28 and 29, 2004, the Panel met on five separate occasions. The usual format consisted of an executive session in the morning, followed by a working lunch with members of the Board Liaison Committee, ending with a second executive session in the afternoon.

As requested by the Board in the September press release, the Panel made its initial recommendations at the Board meeting on January 28, 2004 in Arlington. The memorandum accompanying the January 28 recommendations noted that the Panel's efforts with respect to the Board were now nearing completion, and that it therefore intended to complete its assignment by focusing on TNC's local chapters as well as assisting TNC's new Chair in his efforts to examine TNC's programs from the standpoint of transparency and accountability. The Panel was very pleased that independently of its efforts, Chair Paulson had already begun, at a lengthy meeting on January 9, intensive efforts to study each of the programmatic areas in question, and recommend appropriate changes as necessary with special emphasis on risk and reputation.

The Panel was not established to investigate past practices, but it necessarily had to become aware of them in order to make its recommendations. Accordingly, when the Panel turned its attention to the issues discussed in Part III, it did so recognizing that those issues were within the province of the newly restructured Board. The Panel notes that the Board and senior staff have already made important changes to TNC processes and procedures, and that the process of review and change is fluid and continuing under the Board's supervision. The Panel's discussion in Part III, therefore, is general and intended to be of guidance.

The Panel compliments Chair Paulson, the Board, and the senior staff on the speed and diligence with which they are evolving TNC -- it bodes well for the future.

Since the Panel began its work last year, it has spoken often and at length with a number of people who have been extremely helpful in assisting Panel Members with their deliberations, in addition to extensive interviews with TNC volunteers and staff at all levels, including, of course, Chairs Grassi, Dinkins, and Paulson, and the President and his staff at TNC's world headquarters, all of whom cooperated fully with the Panel and provided the Panel with full and free access to TNC.

The Panel also wishes to express its appreciation for the time and counsel the following individuals provided: Bob Ackerman, Chapter Chair, Massachusetts; Graham Chisholm, State Director, California; Bryant Danner, Trustee, California; Dennis Fitzpatrick, Chapter Chair, Idaho; Tom Harville, Chapter Chair, Washington; Wayne Klockner, State Director, Massachusetts; Geoff Pampush, State Director, Idaho; Wendy Paulson, outgoing Chapter Chair, New York; Jan Portman, Member, Board of Governors; Roy Rogers, Chapter Chair, Florida; Alan Seelenfreund, Trustee, California; Henry Tepper, State Director, New York; Vicki Tschinkel, State Director, Florida; and David Weekes, State Director, Washington.

In a similar fashion, the Panel wishes to thank Milton Cerny, former Chief of Exempt Organizations Rulings of the IRS and Member, Caplin & Drysdale, Washington, D.C.; Jay Erickson, Managing Director, Montana Land Reliance; William Josephson, Assistant Attorney General, Charities Bureau, New York State; Karin Kunstler Goldman, Registration Section Chief, Office of the Assistant Attorney General, Charities Bureau, New York State; Marcus S. Owens, former Director of the Exempt Organizations Division of the IRS and Member, Caplin & Drysdale; Rock Ringling, Managing Director, Montana Land Reliance; Jonathan Selib, Democratic Staff Member, U.S. Senate Finance Committee; Stephen J. Small, Esq., Boston, Massachusetts, and former attorney in the Office of Chief Counsel of the IRS; Mark S. Weston, Real Estate Consultant and Appraiser, Hunsperger & Weston, Greenwood Village, Colorado; Douglas Varley, Member, Caplin & Drysdale; and Dean Zerbe, Chief Investigative Counsel, U.S. Senate Finance Committee.

Finally, the Panel wishes to thank David B. Hird, John A. Neuwirth, and Robert C. Odle, Jr. of Weil, Gotshal & Manges LLP for their invaluable assistance in gathering information and organizing the work of the Panel.

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## I. The Board

The past years have witnessed a dramatic shift in public expectations regarding the accountability of private organizations and the responsibilities of their governing boards. This has involved highly publicized scandals at large for-profit corporations, and media and U.S. Government attention to philanthropic and other non-profit entities. *The Washington Post* series on The Nature Conservancy is illustrative of the trend, but there have been similar reporting and editorial comment in newspapers and magazines throughout the nation. This process is likely to accelerate as Congress examines the manner in which the tax code is currently used by non-profit organizations.

These developments promise to bring new pressures to bear on non-profit boards to become more informed and more active in overseeing their operations. Faced with this changing environment, the Governance Advisory Panel offered a preliminary proposal to TNC's Board of Governors on January 28, 2004. Following a series of lengthy, interactive, and productive meetings with the Board's Liaison Committee; it attempted to outline how TNC might initiate changes at the Board level in its structure and functioning to help it respond more proactively to the challenges that currently confront it. The Board of Governors adopted this proposal at its meeting on January 29, 2004, and since that time, refinements have been incorporated based on comments from TNC officials and others.

The Panel believes that a central issue of board governance is ensuring that the board serves as an active and objective body for monitoring management activities. Because non-profits receive private donations and public benefits, it is essential that a non-profit board ensure that managers use organizational assets for their intended purpose, and scrupulously operate in a transparent, lawful, and ethical manner.

Board duties should include:

- Articulating expectations and standards related to organizational culture and the "tone at the top";
- Establishing the basic policies of TNC and reviewing any proposed deviations from them;
- Selecting, monitoring, evaluating, compensating, and if necessary, replacing the president, and in some circumstances, senior staff;
- Reviewing and approving management's strategic and programmatic plans (consistent with the non-profit mission) and monitoring performance against the strategic and programmatic plans to evaluate whether the organization is being properly managed;
- Reviewing and approving the organization's financial objectives and major plans and actions;

- Reviewing and approving significant transactions;
- Reviewing and approving the auditing and accounting principles and practices used in preparing the organization's financial statements;
- Providing oversight of disclosure and transparency, risk assessment, internal controls, and processes designed to promote legal and ethical compliance; and
- Assessing the board's own effectiveness.

It is in this spirit that the following has been formulated:

- A. The current Board of Governors ("BOG") would select the Members of a new Executive Committee ("EC") to consist of the Chair, two Vice Chairs, President, Secretary/Treasurer, and the Chairs of six Committees, for a total of eleven Members of the new EC. The Chair and the two Vice Chairs would each inform themselves as to the activities of two Committees and would each act as liaison to two committees.
- B. The Committees would consist of approximately five Members each, would be drawn from the entire membership of the BOG, and would meet at least quarterly. The Governance Committee would lead the process by which Members of the BOG are assigned to Committees. The President would not serve on Committees. Because each BOG Member would make a serious and significant commitment of time to Committee work, to the extent practical no one would be expected to serve on more than one Committee, although the Chair could attend any Committee meeting ex officio, as could the President, unless excused by the Members of the Committee. Written charters stressing each Committee's accountability for its missions would be prepared by each Committee, and reviewed annually for submission to the Governance Committee, and then to the EC and the BOG. The Vice Chairs of each Committee, who would serve on the BOG but not on the EC, would be responsible for each Committee's liaison efforts with local chapters. Further, while it is inevitable that the work of one Committee may overlap with that of another, such overlap is not necessarily undesirable.

The Committees would be:

(1) Audit:

- Normal audit functions (retain, evaluate, and work with outside auditors; internal audit function)
- Financial Reporting and Regulatory Reporting
- Compliance (ensuring procedures support policies and monitor compliance with procedures)
- Legal (address broad legal issues that have ramifications across TNC)
- Ethics (compliance with organization's values and code of conduct, including whistleblower issues)

- Compliance with lobbying regulations
- Conflicts of interest

N.B.: At some point in the future, the EC might shift certain of these assignments to other Committees if they result in precluding the Audit Committee from a sharp focus on basic Audit Committee tasks.

(2) Strategy:

- Mission, Strategy, Values
- Strategic and Annual Planning
  - Science, including annual "Science Audit"
  - Measures and Results
  - Public Policy and Government Relations

(3) Governance:

- Nominating
- Orientation
- Board and Committee Self Assessment
- Volunteer Leadership
  - Role of state/country volunteer leaders
  - Relationship of trustees and BOG in governance
  - Engagement of state/country volunteers to maximize influence and reach
  - Standards, Best Practices, and BOG Guidelines
- Human Resources
- CEO evaluation and succession
- Compensation

(4) Conservation Project Review:

N.B.: The purpose of this Committee would be to ensure adequate oversight and risk management of TNC's conservation programs, with a particular emphasis on large or novel conservation projects -- i.e., high-dollar value conservation buyer transactions and transactions with government entities, compatible human use activities, etc. Other functions of this Committee would include:

- Strategic fit/conservation, return on investment
- Risk assessment and management (financial, reputational, legal, and ethical)
- Easements (valuation, monitoring, amendments, enforcement, conservation value)
- Scientific rationale

(5) Finance:

- Investment policy and oversight
- Budgeting
- Long-term financial planning
- Financial status
- Performance benchmarks

(6) Marketing and Philanthropy:

- Donor Relations
- Fundraising Strategy and Results
  - Membership
  - Annual Funding
  - Capital Funding
- Fundraising Efficiency
- Communications
  - Marketing
  - Public Relations

- C. It would be important for some of the EC Members to be persons who are not current Members of the BOG. This would be accomplished as soon as reasonably possible. All BOG Members would participate in an extensive orientation course and the Governance Committee would regularly review BOG Member performance. Over time, some Members who leave the BOG would not be replaced so that the size of the BOG did not increase beyond its current size due to the fact that any person elected to the EC would automatically become a member of the BOG.
- D. Members of the BOG and EC would be independent of TNC pursuant to standards to be established, but at a minimum, no Member of the EC could hold any other TNC position, except for that of President. It would be, however, desirable if some Members of the EC had previously served as trustees.
- E. TNC financial supporters would be eligible for election as BOG and EC Members, but no Member or his/her company could take an income tax deduction for any gift of land to TNC nor could any Member or his/her company purchase land from or sell land or easements to TNC while serving as a Member. Monetary gifts would of course be welcomed but Members and their companies would not be permitted to have cause-related marketing agreements with TNC.
- F. While BOG and EC Members would not be chosen to represent TNC "constituencies," selecting Members who have expertise and competency in various areas in addition to conservation and the environment would be strongly encouraged, especially in governance, but also in other areas such as international affairs, ethics, audit and accounting, finance and investment, tax policy, conservation science, public and governmental affairs, real estate, law, etc.

- G. BOG and EC Members would be elected for staggered three-year terms. Members would be eligible to serve two consecutive three-year terms, and would be eligible for election again one year after serving two consecutive three-year terms.
- H. The EC would have in-person meetings at least quarterly. The EC and the Committees could and would meet telephonically between regular meetings. The BOG would meet two or three times a year, and could meet telephonically. Other than the President, BOG and EC Members would not be compensated.
- I. The Chair would be responsible for the development of the agenda for each EC meeting. The outside EC Members would devote a portion of each meeting to a session which would not include the President.
- J. An independent, outside auditor and the Director of Internal Audit would be appointed by the EC annually upon the recommendation of the Audit Committee and would report to the Audit Committee. The fees for the outside auditor would be set by the Audit Committee. The Audit Committee would decide no less frequently than every five years whether a new outside auditor should be selected, and if the then-current auditor is retained, a new lead partner would be selected. The General Counsel and a new Compliance Director would be selected by the President, subject to the prior approval of the EC. The Internal Audit Director's position description would be expanded to include responsibilities similar to those in U.S. Government departments held by Inspectors General, i.e., an internal investigatory function. The General Counsel and the new Compliance Director would report directly to the EC as well as to the President. Annual audits of legal issues and science programs would be performed.
- K. In the interest of accountability to the internal and external and numerous and varied constituencies that have an interest in TNC, a major focus of the EC would be the promotion of transparency in all facets of TNC's governance, businesses, programs, and performance, including oversight of all mandatory and discretionary reporting.
- L. The new structure would be phased in as soon as possible. Thereafter, the EC would develop formal elaborated guidelines for its future operation and conduct. These guidelines would include, among other things, Committee charters more particularly specifying the respective responsibilities and organization of each of the Committees (including the EC). A draft Audit Committee Charter is annexed to this Report as Appendix B.

## II. The Field

The Panel has focused on TNC's local chapters because it believes that great and enduring enterprises are built around a robust core that defines and drives an institution. In TNC's case, that core is represented by its local chapters. For decades, relatively independent field operations have worked to conserve land, develop membership, engage local trustees, and generate significant financial support – primarily within the boundaries of their separate geographies. The unparalleled success of these chapters sets TNC apart from other conservation organizations, and provides an opportunity for TNC to impact ecosystems throughout the world.

Despite the grassroots nature of the chapters, TNC is organized as a single non-profit entity, reflecting the inherent interdependence of local organizations pursuing a regional, national, and global mission. The operating implications of Conservation by Design, TNC's overarching strategic framework, amplify this interdependence, as does the imperative to minimize organization-wide risk in an era of increasing public scrutiny.

If local chapters are primarily accountable for pursuing TNC's strategy within their boundaries, then the BOG and EC will ultimately be accountable for insuring that the whole is greater than the sum of the parts; that is, enhancing the overall long-term success of the mission, while mitigating its inherent risks. Because TNC is fundamentally chapter-driven, its world headquarters is highly dependent upon the behavior of the chapters – and vice versa. Given TNC's strategy and circumstances, there can only be shared accountability for future outcomes. And because the reputation of each chapter is affected in today's world by the behavior of other chapters, all chapters have a stake in an effective system of standards and accountability administered nationally and coordinated with the field.

The issues of governance, accountability and transparency are complicated for TNC due to its chapter structure. There are currently fifty-five relatively independent chapters in the U.S., each with its own board of local trustees. Although these boards have no real fiduciary responsibility, they are, in practice, highly engaged in the strategy and operations of the chapters. Their activities range from reviewing land transactions, fundraising, approving budgets, advising local staff on various management issues, and actively participating in the hiring of the State Director. Some trustees have served in this role for many years, while others are new to TNC. As a group they number approximately 1,500 and represent an essential asset in pursuit of TNC's mission to preserve the world's last great places.

TNC's historic growth and success can be traced directly back to the achievements of these chapters. What began in 1951 as a local effort in New York State to preserve parcels of land grew to encompass twenty state chapters by 1975. In the following decades, grass roots efforts were supplemented by a more proactive strategy as TNC expanded internationally in places such as South and Central America, the Caribbean, the Pacific Rim, Canada, and China. TNC's ability to blend strong local presence with centralized leadership and collaboration has been essential in protecting ecosystems that naturally transcend state and regional boundaries. Nevertheless, to the broad range of members, TNC has been very much "placed based," with particular enthusiasm centered on projects which are generally close to home. It is a great strength of the organization that so many members think of it as "my TNC."

This organizational approach also explains why TNC is structured as a single 501(c)(3) entity. The Panel examined other large geographically diverse charities and found that most are organized as a “federation” of separate legal entities (examples include: The United Way, Habitat for Humanity, Catholic Charities, and the Boy Scouts of America). Although this federation approach may help clarify the accountability and role of local directors, there is no evidence that it significantly improves overall governance of the entity.

On balance, the Panel is convinced that TNC’s local chapters form the fundamental core of TNC’s operations, and that those chapters should continue to be integrated within the boundaries of a single 501(c)(3) entity.

In that context, the Panel evaluated actual governance practices of a cross section of TNC chapters. We found the local trustees to be extremely competent, highly engaged and committed to TNC’s success, and in general agreement about TNC’s overall strategic direction. “Conservation by Design” had wide support among local trustees and staff. That said, the inherently grass roots and independent nature of the chapters led to many inconsistencies relating to governance practices. No single inconsistency was particularly alarming; in general, chapter trustees are well organized and productive. However, there were a number of variations around the exact role of the individual trustees, the structure and functioning of local “boards”, the application of by-laws, and the participation in local decision-making (both strategic and operational).

Given our recommendations concerning TNC’s Board, and our understanding of local chapter governance within TNC, the Panel proposes three areas for improvement:

- Establish minimum uniform governance standards for each chapter trustee board;
- Clarify decision making roles and responsibilities between the BOG, EC, local chapter boards, and senior staff, especially as pertains to land transactions and strategic decisions; and
- Enhance transparency and communication between the BOG, EC, and chapter trustees and staff.

We briefly elaborate on each of these recommendations below:

A. Governance Standards for Chapter Boards

Minimum standards should build upon a combination of historic best practices and the restructuring of the Board. The following areas should be addressed:

- Committee structure, membership, and charters
- Audit and evaluation practices
- Eligibility and participation requirements for chapter trustees
- Terms and term limits
- Minimum meeting requirements
- Reporting requirements
- A trustee orientation/training program

This process should produce an updated set of chapter by-laws and a process for evaluating compliance across all TNC chapters.

#### B. Decision-Making Roles and Responsibilities

While TNC should continue to promote innovation and entrepreneurship by the chapter boards, the Panel believes that ultimate authority should remain with the BOG and the EC, which are responsible for supervising the actions of the chapter boards and reviewing their decisions.

The Panel believes that chapter boards should review and ratify the most important decisions confronting local chapters, subject to the ultimate authority and oversight of the BOG and the EC. These decisions should parallel the types of decision made at the BOG and EC level as well as the standards for making such decisions, and would likely fall in the following categories:

- Chapter strategy, particularly its alignment with TNC's overall strategy
- Operations: e.g., approval of annual budgets, hiring targets, financial plans, fundraising practices
- Land transactions: e.g., any and all potentially "high risk" transactions
- Compliance with policies and procedures: e.g., TNC-wide policies requiring chapter compliance such as conflict of interest

By specifying that certain decisions must be debated and approved by chapter boards, TNC will encourage accountability of local leadership, improve the quality of its decisions, and enhance its ability to effectively govern its complex organization. And, of course, significant decisions of chapter boards must be subject to review by world headquarters to insure consistency.

#### C. Transparency and Communication

Given the need for greater coordination and integration between the BOG, EC, and chapter trustees, it is the Panel's recommendation that TNC identify mechanisms to insure better transparency and communication among the various leadership groups. While current practices are admirable, they fall short given the growth of TNC, the dynamics of its environment and the new pressures surrounding non-profit boards to be more diligent in the oversight and evaluation



of operations. At least in the short term, TNC should do its best to over-communicate regarding any significant issues, initiatives or decisions.

Of course, there are inherent tensions between the center and its constituent parts in every organization with strong local units; this can best be minimized through ample coordination and exchange of information.

These three sets of recommendations around chapter governance standards, decision-making, and communication are intended to complement the Panel's recommended modifications to the Board, while reinforcing the changes to policies and procedures that have and will be made.

These recommendations regarding the functions of the chapters and their interaction with world headquarters are key to the future credibility and efficiency of TNC. Implementation of these necessarily generic recommendations obviously will take a great deal of time, goodwill, effort, and forthright communication.

The EC must assume this responsibility promptly, and with special effort, in the hope that within a reasonable time concrete policies and processes will be in place that adhere to these general principles.

### III. Programs, Transparency, and Accountability

In addition to recommendations concerning the issues addressed in Parts I and II of this Report, the Panel's charter also requests recommendations on ways to improve and enhance TNC's transparency and accountability, particularly as these issues relate to TNC's programs and policies.

Progress continues with steps taken by TNC's new chairman, Henry M. Paulson, Jr., and by the senior staff. Shortly after his election, Mr. Paulson convened on January 9, 2004, an "issues meeting" of TNC senior staff members to discuss proposed changes to, and risks posed by, TNC's policies relating to conflicts of interest, easements, land transactions with government, project review, compatible human use, and compensation. This ongoing process of review and change at TNC is comprehensively documented in a February 12, 2004 memorandum prepared by TNC Managing Director of External Affairs, Michael Coda, entitled "Processes for Managing Reputational Risks" (the "Memo"). The Panel believes the Memo represents a substantial effort by TNC's senior staff to develop policies and practices to address many of the key issues of transparency and accountability facing TNC. The Panel notes that the Memo has undergone a series of revisions reflecting the progress TNC is making with regard to the identification of issues and appropriate ways to address these issues.

Given the ongoing modifications that TNC is making in these areas, and as discussed in the Introduction, the Panel's comments are necessarily general.

#### A. Valuations and Appraisals in Land Donations and Conservation Easements

Land donations and conservation easements play a critical role in TNC's mission. For many years, TNC has appropriately measured the success of its efforts in terms of the number of acres of ecologically sensitive land held in fee or controlled through easements.

Clearly, the availability of a federal tax deduction is a major incentive for donors to contribute land or easements to TNC. Although current law requires TNC, as the donee organization, to acknowledge receipt of the gift on IRS Form 8283, it does not require that TNC take a position on the value of the gift. In the past, TNC's policies have been consistent with the law: TNC would not take a position on the value or deductibility of any easement or gift of land; TNC would undertake its own appraisals usually for the purpose of determining whether the sale price which TNC paid or received for land or easements were supported, but not to determine the propriety of the donor's appraisal.

Recently, however, concerns have been raised -- also appropriately -- about the validity of appraisals used to support the claims for tax deductions made by donors of land and easements to non-profits. Given the understandable concerns about valuations and donor contributions to non-profits, the Panel recommends that TNC put in place careful, systematic, and strict procedures that will ensure compliance with all aspects of the spirit and letter of the rules for charitable contributions of conservation donations, with particular emphasis on appraisals and other elements of valuation substantiation of such gifts.

The Panel applauds the recommendations of the senior staff in the Memo which propose that TNC refuse to sign a Form 8283 unless the donor's appraiser is state-certified, not barred from practicing before the IRS, and has experience appraising conservation lands and easements. The Memo also recommends that TNC determine that the appraiser uses generally accepted professional appraisal standards, accounts for the enhancement to any neighboring property owned by the donor, and certifies his or her awareness of any conflict of interest. The Panel considers these recommendations to be important steps in the right direction.

The Panel suggests that potential donors be informed at the outset of the transaction that TNC will closely examine the qualifications of the appraiser, the methods used, and the appraisal itself.<sup>1</sup>

In addition, the Panel recommends that TNC undertake a "desk review" of all aspects of a proposed conservation transaction, which would include a review of the donor's appraisal, to determine whether the transaction is appropriate.

The Panel believes that TNC must demonstrate that it is willing to "walk away" from an otherwise advantageous transaction where all aspects of the transaction do not meet TNC's new standards, including where a donor wishes to claim a tax deduction based on an appraisal that is not justified.

Finally, the Panel notes that the Memo (at p. 24) recommends training in TNC compliance policies, which the Panel certainly encourages; the Panel recommends that such training be expanded to cover tax issues relevant to both TNC and donors. The Panel also suggests that TNC encourage law and business schools to include these subjects in courses.

#### B. Monitoring and Enforcement of Easements

A closely related issue is the monitoring and enforcement of easements. The conservation value of easements could be undermined if property owners do not comply with the terms. Moreover, adequate monitoring and enforcement of easements is critical to achieving long-term conservation results. The Panel believes that TNC should regularly monitor compliance with easements, should require property owners to disclose plans for changes in easements, and take rigorous enforcement action where landowners act inconsistently with easement terms.

TNC recognizes these concerns, and in addition to the easement policy it adopted in 2001, the Memo (at pp. 22-23) sets forth several proposals for ensuring more effective monitoring and enforcement of conservation easements. The Panel recommends that TNC's General Counsel and its Compliance Director take steps to implement programs to enforce the easement amendment policy and take aggressive action, where appropriate, against land owners who infringe upon easements.

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<sup>1</sup> TNC should consider whether the review of the donor's appraisal could take place at the time the gift is made, not after the fact when the Form 8283 is submitted. Because the Form 8283 need not be completed before the donor files a tax return, it may not be submitted for many months (especially if the taxpayer seeks an extension of the filing date) after the end of the calendar year in which the donation was made.

### C. Conflicts of Interest

At TNC's June 2003 Board of Governors meeting, the Board modified TNC's conflicts of interest policy to prohibit the purchase or sale of land, easements or any other interests in land involving members of the Board, trustees and employees (and their immediate families). In addition, the Board made clear that parties entering into land transactions with TNC must be unrelated to TNC for a minimum of one year before entering into a land transaction.

Following these changes, at the January 29, 2004 Board of Governors meeting, the Board adopted the Panel's Proposal requiring that no member of the Board or Executive Committee of the Board (or his or her company) (i) take an income tax deduction for any gift of land to TNC; (ii) purchase land from, or sell land or easements to, TNC; or (iii) have a cause-related marketing agreement with TNC.

Additional improvements to TNC's conflicts of interest policy are comprehensively set forth in the Memo, including one that "major donors" be considered "covered persons" and, thus, subject to the policy. The Panel understands that TNC is in the process of redefining the term "major donor" for purposes of conflict of interest analysis to include anyone who donated cash or assets worth \$100,000 or more in the aggregate during the five years prior to the transaction.

It is especially important that the Audit Committee remain actively involved in overseeing and monitoring TNC's policies and procedures with respect to conflicts of interest, and that TNC's conflicts of interest policy be transparent (i.e., clearly articulated in TNC's Form 990 which would, in turn, be posted on its website).<sup>2</sup>

### D. Transactions with Governmental Entities: the "No Net Profit" Policy

The Panel believes that it is important for TNC's reputation that not only it comply with its "No Net Profit" policy, but also be able to document that compliance in a transparent manner.

The Panel recommends that the "No Net Profit" policy be fully disclosed on its Form 990. In order to achieve even greater transparency, the Panel further suggests that TNC consider whether to publicly disclose the actual prices paid and received by TNC in transactions involving government entities.

The Panel believes that the Memo properly articulates the specifics of TNC's "No Net Profit" policy, and explains how to calculate the sales price in order to comply with that policy.

### E. Compatible Human Use

TNC has long recognized that conservation of biodiversity must allow for a reasonable amount of human use of conservation lands. It is important that TNC be able to demonstrate that

<sup>2</sup> The Panel agrees with the recognition in the Memo (at p. 12) that "having a sound Conflict of Interest Policy will help The Nature Conservancy comply with the Standards for Charity Accountability established by the BBB Wise Giving Alliance, with Internal Revenue Service rules against private inurement and private benefit, and with state statutes addressing conflict transactions."

it is consistently following a policy of allowing only those human uses that are compatible with TNC's conservation goals and adhere to it.

In this regard, at the June 13, 2003 Board of Governors meeting, the Board affirmed that human use on TNC preserves may occur in four circumstances:

- The activity has little predicted impact and poses no identified threat to TNC's conservation targets;
- The activity has limited predicted impact but has an educational or other value that outweighs the predicted impact;
- The activity is part of a strategy to reduce or eliminate threats to conservation targets or is designed to mimic or restore essential ecological processes; or
- The activity contributes significantly to learning and demonstration opportunities for compatible use and biological diversity preservation when weighed against potential impacts.

The Board also (i) resolved that TNC will not initiate new oil and gas drilling or mining of hard rock minerals on TNC preserves unless already required by existing contracts; and (ii) organized a team of Board members and independent ecologists and economists to advise on human use activities. The team of Board members, ecologists and economists submitted a report to the Board in October 2003, focusing on the need for a greater scientific understanding of the impacts of proposed human uses and their financial implications. The report also addressed issues regarding appropriate levels of decision making and governance with respect to human use activities.

The Panel believes that the Board's articulation of TNC's compatible human use policy on June 13, 2003 is appropriate. In addition, the Panel agrees with the recommendation in the Memo that a committee composed of senior staff be formed to review "innovative, large scale, or untested proposed human uses." The Panel would also suggest that any proposed transactions approved by this committee be presented to the newly-formed Conservation Project Review Committee for final approval. For purposes of transparency, the Panel recommends that TNC also include an explanation of its compatible human use policy, with examples, in its Form 990.

#### F. Executive Compensation

In recent years, executive compensation at for-profit organizations has come under intense scrutiny. If anything, this issue is even more sensitive in the context of not-for-profit organizations. Both for purposes of public perception and for maintaining its tax-exempt status, TNC should maintain a consistent policy of paying executives amounts comparable with those paid by other similar not-for-profit organizations. It is especially important that the Governance Committee play an active and independent role in reviewing the performance and setting the compensation of the President, as well as reviewing and approving the compensation of senior

staff positions; and the compensation of the President and senior staff should be disclosed in great detail in the Form 990. Any compensation consultant retained by TNC should be chosen by the Committee.

The Panel could not agree more with the statement in the Memo (at p. 5) that "it is important to ensure that TNC has a well-structured and transparent policy toward determining compensation levels for its senior executives." Accordingly, the Panel recommends that the EC adopt the suggestions of the TNC Compensation Working Group (outlined on pp. 5-6 of the Memo) with respect to the manner in which the new Governance Committee should oversee matters of senior management compensation.

#### G. Lobbying

In order to maintain its tax-exempt status, section 501(c)(3) organizations such as TNC are required under the Internal Revenue Code to limit their lobbying activities to less than a "substantial part" of their overall operations. In this regard, as noted in the Memo, the TNC Board of Governors has approved an expenditure of up to only two percent of TNC's charitable budget on lobbying activities. The Panel believes that this threshold is more than consistent with the letter and spirit of IRS policies.

#### H. Compliance

The Panel's recommendation that TNC hire a permanent Compliance Director was adopted by the Board at the January 29, 2004 meeting, and the Memo properly articulates the responsibilities attendant to such a position.

Unlike the Internal Auditor whose function would be to review past events and transactions, the Compliance Director would essentially operate on a going-forward basis. The Compliance Director would implement programs to ensure that TNC operates in accordance with the law and its policies, and would review specific transactions and events as they transpire for adherence to the law and TNC policies. By contrast, the Internal Auditor's role would be to review completed transactions and events, in addition to duties such as those of an inspector general in a government agency, which also involve the review of completed transactions and events.

In the Memo (at p. 8), senior staff has suggested that the Compliance Director be housed in the office of TNC's General Counsel, and report to both the General Counsel and the Audit Committee. As set forth in the Panel's Board Proposal, the Panel recommends that the Compliance Director report directly to the EC as well as to the President. In addition, while the Panel recognizes that the costs of establishing the new position of Compliance Director will be significant, the Panel does not believe the Compliance Working Group should specify in advance that the Compliance Director should have no additional direct reports other than an administrative assistant. The Panel recommends that the Compliance Director be recruited from outside TNC.

## I. Reputation and Transparency

In addition to the recommendations made above with respect to individual issues, the Panel has observations involving generic questions of reputation and transparency. The first concerns establishing mechanisms to review conservation projects before committing to them in order to ensure that they not only meet TNC's conservation objectives and comport with its policies, but do not raise issues of compliance or reputational risk. The second concerns using TNC's IRS Form 990 as a voluntary disclosure device in order to promote transparency.

### (1) Conservation Project and Activity Review

The Panel's Proposal in Part I recommended the creation of a Conservation Project Review Committee of the EC to ensure adequate oversight and risk management of TNC's conservation programs, with a particular focus on large or novel conservation projects. For example, the Conservation Project Review Committee would closely examine high-dollar value conservation buyer transactions and transactions with government entities, as well as proposed compatible human use activities. The Panel believes as does the BOG that such EC level review is essential to protect TNC's reputation, assure legal compliance, and serve the organization's conservation objectives.

The Memo proposes to augment the work of this Committee by creating processes for managing risk at the staff level (Memo at pp. 33-36), including the proposed creation of a staff level committee to oversee such processes (which committee itself would report to the Conservation Project Review Committee). The Panel agrees with this approach which should go a long way toward achieving this end and preventing any single project from damaging TNC's reputation.

### (2) TNC's Form 990

The Panel believes that the Form 990, which the Internal Revenue Service requires all non-profits to file annually, provides an opportunity for transparency and disclosure. Although the Form 990 does not require disclosure as detailed as that required in annual reports filed by public companies with the Securities and Exchange Commission, it can serve as a non-profit's version of what is now required by Sarbanes-Oxley for public companies. Therefore, the Panel suggests that TNC voluntarily disclose as much as possible (about its mission, policies, programs, goals, etc.) in its annual Form 990 in order to keep donors, the public, and interested governmental entities well informed about its activities. The Panel suggests that the changes and initiatives implemented since the June 13, 2003 BOG meeting be discussed in TNC's next Form 990, and that thereafter each Form 990 should include a report on the work of the Conservation Project Review Committee during the prior year.

The Panel observes that the Form 990 filed by Memorial Sloan-Kettering serves as an example of a model Form 990.

Simply put, TNC could use its Form 990, in the words of one commentator, "to detail the activities, experiences, and ethical record of the organization during the previous year."

## Appendix A: Work of Outside Advisors on Key Issues

August 20, 2003

The Nature Conservancy aspires to set a standard for best practices for a highly-decentralized, global non-profit organization, committed to a culture of innovation through competent risk taking. While confident that TNC has the right values and strategy to serve its mission, the Board is constantly seeking to improve and enhance its governance, transparency, and accountability. Therefore, the Board decided at its meeting on June 13, 2003 to enlist outside perspective and expertise to help in these areas. This memo will further define this work.

The objective of the work with independent advisors will be to provide the Board of Governors of TNC with a set of forward-looking recommendations on key issues facing the organization in the areas of governance, transparency, and accountability.

The outside advisors will be given latitude in determining the scope of their work with the caveat that we are not looking for an evaluation of the past but rather advice on how to move forward in the areas of governance, transparency, and accountability. This Governance Advisory Panel will be chartered by the Board of Governors and the group will deliver the recommendations to the Board and keep the Board informed throughout the group's process. The Panel will have the opportunity to make recommendations related to other issues discussed at the June 13 Board meeting but its focus will be on questions that were not addressed or remain unresolved after that session. These outside advisors will not be staff or Board members of TNC. The outside advisors will be asked to serve pro bono, however they will be reimbursed for their expenses. A final report of the Panel's recommendations will be made available to the public.

The group will include up to seven individuals with diverse and broad experience in the issues of governance, both in the for-profit and non-profit arenas. These individuals will have a reputation for integrity and a commitment to conservation. The Panel will be fully supported by professional staff hired for this purpose. TNC will raise funding to cover the costs of this staff.

The Panel will make an interim report to the TNC Board at its meeting in January. It is anticipated that final recommendations will be made by March, 2004. The advisors will be asked to develop answers to a series of questions. These questions are drawn from the discussion of the Board of Governors at the June 13 Board meeting. The questions are in the following areas.

### Governance

The Board would like the outside advisors to provide their advice on how the Board ensures that we use our governance processes to achieve the highest levels of integrity throughout the organization. Some questions the advisors might choose to address are:

- How can the Conservancy's governance approach better ensure that it achieves its foremost value - integrity beyond reproach?



- What types of backgrounds and experiences should be reflected on the Board of Governors and in what proportion to the total Board membership? How many members should the Board have? Should there be any other entities created (i.e. advisory councils) to help the Board do its work?
- What is the optimal committee structure arrangement and what should be the charges to those committees?
- How should issues be identified for Board consideration and review?
- How should potential Board members be identified?
- How does the Board ensure that our procedures are designed and executed so as to support the policies established by the Board?

### Transparency

We would like the advisors to give us their opinion on the meaning of transparency in the non-profit sector and how to apply this perspective within the context of TNC. Some questions the advisors might choose to address are:

- What can TNC do to reach its desired standard of becoming a model of transparency in the non-profit sector?
- What categories of information should be easily available to all the constituencies that are important to TNC?
- How do we ensure there is no gap between how we describe ourselves and who we really are?

### Accountability

We are seeking assistance in thinking about the issue of accountability. To what constituencies are we accountable and how are we accountable? Other questions the advisors might provide an opinion on are:

- What are the key areas in which the Board of Governors needs to step up its oversight of TNC activities in order to minimize risk to the organization?
- What benchmarks should the Board establish to monitor the organization's performance?
- What role should members, donors, and partners play in evaluating TNC's effectiveness?

## **Appendix B: Draft Audit Committee Charter**

As New York State Assistant Attorney General William Josephson has noted, in today's world the Audit Committee is the sine qua non of a non-profit. The Panel agrees, has emphasized the importance of the Audit Committee in Part I of this Report, and has also prepared the following draft charter for the EC's consideration.

### **Purposes**

The Audit Committee will assist the BOG and the EC in fulfilling its oversight responsibilities by monitoring (1) the overall systems of internal control and risk mitigation; (2) the integrity of the financial statements of TNC; (3) compliance by TNC with legal and regulatory requirements and ethical standards; and (4) the independence and performance of TNC's internal and independent auditors.

### **Membership and Meetings**

Committee members shall have a basic understanding of finance, accounting and fundamental financial statements, and at least one member of the Committee shall be a financial expert as determined by the EC.

The Committee shall meet quarterly with the internal auditor and twice each year with the independent auditor in separate executive sessions to provide the opportunity for full and frank discussion without members of senior management present.

### **Authority**

The Committee's role is one of oversight. TNC's management is responsible for preparing TNC's financial statements and the independent auditors are responsible for auditing those financial statements. The Committee recognizes that TNC's management, the internal audit staff and the independent auditors have more time, knowledge, and detailed information about TNC than do the Committee members. Consequently, in carrying out its oversight responsibilities, the Committee is not providing any expert or special assurance as to TNC's financial statements or any professional certification as to the independent auditor's work.

The Committee shall have the power to conduct or authorize investigations into any matters within the Committee's scope of responsibilities, with access to all books, records, facilities and personnel of TNC. The Committee shall have the power to retain special legal, accounting, or other consultants to assist in the conduct of such investigations or to advise the Committee, at TNC's expense and without further BOG or EC approval.

The Committee may request any person, including but not limited to any officer or employee of TNC or the independent auditor, to attend Committee meetings or to meet with any members of, or advisors to, the Committee.

## Responsibilities

The Committee shall undertake the following responsibilities, which are set forth as a guide. The Committee is authorized to carry out these activities and other actions reasonably related to the Committee's purposes or assigned by the BOG or EC from time to time.

### *Internal and Independent Audits*

#### *Internal Audit*

- Recommend the appointment, compensation, performance evaluation and replacement of the Director of Internal Audit, who shall report functionally to the Audit Committee;
- Review the risk assessment that drives the internal audit plan and annually approve the plan;
- Review the activities of the internal audit function; and
- Review the effectiveness of the internal audit function including staffing.

#### *Independent Audit*

- Recommend the appointment of the independent auditor, and evaluate, compensate, and oversee the work of, and if appropriate terminate, the independent auditor, who shall report directly to the Committee;
- Review and approve the terms of the independent auditor's retention, engagement, and scope of the annual audit, and pre-approve any audit-related and permitted non-audit services (including the fees and terms thereof) to be provided by the independent auditor;
- Review and confirm the independence of the independent auditor annually by obtaining and reviewing a report from the independent auditor delineating all relationships between the independent auditor and TNC and discussing with the independent auditor any such disclosed relationships and their impact on the independent auditor's independence and by obtaining the auditor's assertion of independence in accordance with professional standards;
- At least annually, review a report from the independent auditor describing the auditing firm's internal quality-control procedures and any material issues raised by the most recent quality-control review of the firm, or by any inquiry or investigation by governmental or professional authorities, within the preceding five years, with respect to one or more independent audits carried out by the firm, and any steps taken to deal with any such issues; and

- Review with the independent auditor any problems the auditor has encountered performing the audit and any management letter provided and TNC's response to that letter, and matters that the independent auditor is required to communicate to the Committee.

#### *Internal Control and Risk Mitigation*

- Review with management and the independent auditor TNC's major financial risk exposures and evaluate the steps management has taken to monitor and minimize such exposures;
- Monitor the effectiveness of TNC's internal control systems, review, including through regular executive sessions, whether internal control recommendations identified by internal and independent auditors have been implemented by management, review annually the ethics code of TNC and the effectiveness of the procedures established to monitor compliance at every level and ensure through inquiry and other appropriate means that management is communicating the importance of the organization's values, code of conduct and ethics, and internal controls;
- Review adherence to the conflicts of interest and related entities policies, and recommend action as appropriate; and
- Establish procedures for receiving, retaining and treating complaints received by TNC regarding accounting, internal accounting controls or auditing matters and the confidential, anonymous submission by employees of TNC regarding questionable accounting or auditing matters.

#### *Financial Reporting*

##### *General*

- Review with the independent auditor significant accounting and reporting issues, and alternatives, including recent professional and regulatory pronouncements, understand their impact on the financial statements and ensure that all such issues have been considered in the preparation of the financial statements; and
- Review with the general counsel, management and the independent auditor, including in separate executive sessions, key functional activities of TNC, including legal, tax, or regulatory matters that may have a material impact on the financial statements and any material reports or inquiries received from regulators or government agencies.

##### *Annual Financial Statements*

- Review with management and the independent auditor any complex and/or unusual transactions;

- Review with management and the independent auditor, including in separate executive sessions, issues related to judgments made involving valuation of assets and liabilities and commitments and contingencies;
- Review with management and the independent auditor, in separate executive sessions, the annual financial statements and the results of the audit;
- Review with management the annual audit report and recommendations of the independent auditor, including any audit problems or difficulties and management's response; and
- Meet annually with management and the external paid tax preparer to review any issues or judgmental areas relating to the disclosures in TNC's IRS forms.

#### *Compliance with Laws, Regulations, Ethics, and Policies*

- Conduct an annual review of TNC's compliance with law, and with its ethical standards and policies;
- Review with management, including the General Counsel and Compliance Director, all legal and ethical compliance issues;
- Oversee the functions of the Compliance Director;
- Act on findings of the Compliance Director with respect to issues of non-compliance;
- Review with management and the independent auditor, including in separate executive sessions, the findings of any examinations by regulatory agencies; and
- Review with the internal auditors any possible areas of noncompliance with laws and ensure that management follows up with relevant procedures where appropriate.

#### *Conflict of Interest*

- Review, with the General Counsel and Compliance Director, all issues of conflict of interest;
- Coordinate, with the Conservation Project Review Committee, the resolution of conflict of interest issues with respect to conservation projects; and
- Oversee compliance with TNC's conflict of interest policy.

#### *Other Responsibilities*

- Ensure that significant findings and recommendations made by the internal and independent auditors are received and addressed by management on a timely basis;

- Annually review and update the Committee's charter, as needed;
- Conduct an annual performance evaluation of the Committee and make any changes to the Committee's composition or function necessary to address areas of improvement revealed in the evaluation; and
- Maintain minutes of meetings and periodically report Committee actions and make such recommendations as the Committee deems appropriate.

## **Appendix C: Curricula Vitae of Governance Advisory Panel Members**

**Ira M. Millstein (Chair):** Mr. Millstein is a senior partner of Weil, Gotshal & Manges LLP, an international law firm based in New York City. He has counseled numerous high-profile publicly-held corporate boards and state and private philanthropic boards on issues of corporate governance. He is the Honorary Chairman of the Board of Advisors of the International Institute for Corporate Governance at the Yale School of Management and a Professor at the Yale School of Management. He is an elected member of the American Academy of Arts and Sciences and author of books and articles on Corporate Governance.

**Derek C. Bok:** Mr. Bok, a former president of Harvard University and Dean of the Harvard School of Law, now serves Harvard as the Chair of the Hauser Center for the study of nonprofit organizations and philanthropy. He is the author of numerous books on higher education, government, and executive and professional compensation.

**Claudine B. Malone:** Ms. Malone is President of Financial and Management Consulting, Inc. She serves or has served on the Boards of several large companies, non-profit organizations, and academic institutions. She is a former chairman of the Federal Reserve Bank of Richmond.

**Richard T. Schlosberg III:** Mr. Schlosberg is the immediate past president and CEO of the David and Lucile Packard Foundation, a position he held since May 1999. Prior to joining the foundation, he served 23 years in the communications business and was publisher and chief executive officer of the Los Angeles Times and executive vice president of The Times Mirror Company.

**Thomas J. Tierney:** Mr. Tierney is the former chief executive of Bain & Company, an international consulting firm, recognized as one of the premier strategy consulting firms in the world. He is also the founder and Chairman of The Bridgespan Group, an independent, non-profit affiliate of Bain & Company designed to provide high-quality consulting services to foundations and non-profit organizations. He serves on the boards of several non-profit organizations and co-authored Aligning the Stars, an organization and leadership book published by the Harvard Business School Press in 2002.

October 27, 2004  
Senate Finance Committee Letter

Question 20: Narrative Re: Board Approval of Related Organizations

***Many of the most serious Federal tax issues involving an exempt organization can arise when the exempt organization participates in a joint venture arrangement in which it does not own a controlling interest in the venture. Under TNC's recently adopted policies regarding related organizations and significant business holdings, approval of such ventures seems to rest with the President of TNC, rather than with the TNC Board of Governors. Is that a correct understanding, and if so, why is Board approval not required in such instances?***

As described more fully in TNC's prior submissions to the Committee, TNC's specific activities are undertaken pursuant to policies adopted by the Board of Governors or standard operating procedures adopted by TNC's senior leadership team either to implement Board policies or to prescribe standards for activities that may be undertaken without advance case-by-case approval by the Board.

TNC's current policy on Related Entities (copy enclosed) was adopted by the Board on January 30, 2004. It requires that relationships with any entity in which TNC acquires a controlling interest, or where TNC is authorized to act on behalf of such an entity, must be approved in advance by the Board on a case-by-case basis. This is true whether the relationship results from a gift or bequest, a purchase of an interest in an existing entity or the creation of a new entity and the policy applies with respect to a broad range of entities. The covered entities include, but are not limited to, wholly-owned or controlled non-profit corporations; owned or controlled for-profit entities; partnerships and joint ventures; trusts; or other arrangements where TNC acts as a financial fiduciary or agent for another organization, coalition or entity which is otherwise conducting its activities under the auspices of TNC. Under generally accepted accounting principles, these entities are generally treated as a part of TNC and their financial statements generally must be consolidated with those of TNC. As a result, Board approval is necessary and Board considerations are governed by all relevant factors, including those set forth in the policy.

A written standard operating procedure (copy enclosed), also adopted on January 30, 2004, and approved by TNC's Board of Governors, governs cases in which TNC acquires significant business interests in separate legal entities that are not controlled by TNC. Under this procedure, entitled Significant Legal Interests in Separate Legal Entities, such acquisitions may be approved by the President of TNC, subject to a reporting obligation to the Board. As set forth in the procedure, the President's discretion is not unfettered. The approval process must take into account all relevant factors, including those specified in the procedure such as: consistency with TNC's mission, strategy, and values; financial, legal and other costs and risks; tax and other legal and financial reporting implications; and public perception. While the financial statements of entities covered by



this procedure are not consolidated with those of TNC, the procedure does require that the President and Chief Financial Officer specifically apprise the Board where any such interests pose significant potential financial, legal or other risks to TNC.

The absence of a requirement for advance Board approval of non-controlling interests in entities reflects a variety of factors. First, and foremost, in such situations, TNC does not have the right to exercise control over the activities of the entity involved, but is instead responsible primarily to determine that TNC's investment is consistent with its exempt purposes and thereafter to oversee the financial investment. Second, experience has demonstrated that the volume and time-sensitivity of many such investments is such that advance Board approval may be impractical as well as unnecessary. Third, as discussed below, the acquisition of such non-controlling interests may trigger special review by TNC's newly established Risk Assessment Committee and, consequently, by the Board.

As described more fully in TNC's prior submissions to the Committee, TNC has created a Risk Assessment Committee comprised of its senior staff, including the General Counsel and the Chief Ethics and Compliance Officer, among others. The Risk Assessment Committee's organizing documents (see attached memo) contemplate that the Committee will conduct advance reviews of all projects and transactions, including the acquisition of non-controlling interests in other entities, that meet its criteria for review (e.g., transactions or investments that are new, novel or particularly complex; as well as those that comply with all applicable legal and tax law requirements, and with TNC's policies and procedures, but nevertheless involve potentially substantial financial, legal, ethical or reputational risk to TNC). The Board of Governors oversaw the creation of the Risk Assessment Committee, and the Board through a committee thereof -- specifically the Project and Activities Review Committee -- receives reports of all actions of the Risk Assessment Committee.

The policies and procedures described above followed a comprehensive review of TNC's governance by its Board, senior staff and outside experts. These policies and procedures are intended to ensure that all considerations, including the Federal tax issues referred to in the Committee's question, are addressed in advance in the case of non-controlled as well as controlled separate entities. In this connection, it should be emphasized that the procedure governing investments in non-controlled entities does not preclude the Board, in the exercise of its oversight functions, from directing at any time that TNC dispose of any investment made in accordance with the procedure.

Question 21: Narrative Re: Related Organizations

***Please explain how the revised TNC policies regarding related organizations and significant business interests would apply to arrangements such as the GM-TNC emissions arrangement?***

TNC's current policies and procedures with respect to the acquisition of interests, both controlling and non-controlling, in separate entities are described above (Question 20). In the case of the TNC-GM emissions arrangement, regardless of the characterization of the nature of TNC's investment therein at the time of the transaction, under TNC policy and procedures then in effect, prior approval of the Board of Governors acting through its Executive Committee, was sought and obtained.

Were this project to come before TNC's Board of Governors today under the previously described policy and procedure, since TNC's interest in such entity most likely would be characterized as a joint venture, the applicable and relevant TNC policy would be the policy on Related Entities. The reasons for this conclusion are: (1) the venture is established by a formal legal agreement with another party where TNC is a named partner in an ongoing conservation operation; (2) TNC has a controlling interest in the venture by virtue of its ability to veto decisions with respect to the expenditure of funds; and (3) TNC is acting as a "financial fiduciary" with respect to the management and oversight of the funds of this venture. Therefore, TNC's involvement in such an entity would require prior Board approval, as was obtained for the project originally.

Given that the primary purposes of the TNC-GM emissions agreement are to "... promote the protection of plants and animals, sequester carbon from the atmosphere, otherwise reduce so-called greenhouse gases in the atmosphere and achieve sustainable development through community conservation. . ." and in light of the fact that that the funds were intended to be (and were, in fact) used to acquire, manage and restore important habitat in the Brazil Atlantic Rainforest Restoration project in the Guaratuba region of Brazil, an area of recognized biodiversity importance and designated as a UNESCO world biosphere reserve, it is likely that the project would have met the criteria for approval for the Conservancy's involvement in this project under the Conservancy's current policy and procedure.

June 18, 2004

**The Nature Conservancy  
Strengthened Governance, Policies and Procedures**

The mission of The Nature Conservancy is to preserve the plants, animals and natural communities that represent the diversity of life on Earth by protecting the lands and waters they need to survive. This mission is pursued through a science-based planning process called “Conservation by Design”, which enables the Conservancy to identify lands and waters for inclusion in its conservation programs and then design site-specific strategies for the protection of those lands and waters while preserving compatible human uses.

The Conservancy has been and remains committed to carrying out this mission in accordance with the letter and spirit of all applicable laws and its organizational values, which speak to “integrity beyond reproach.” In recent years, the Conservancy has grown substantially, both in absolute size and in the number and complexity of the transactions it undertakes to carry out its conservation mission. The Conservancy has also become increasingly decentralized, operating with professional staff in every state in the U.S., and in twenty-eight other countries. During this same period, policymakers and others have properly focused increased attention on the governance and activities of non-profit organizations, including the Conservancy.

In June 2003, the Conservancy initiated a comprehensive effort to strengthen its general governance and its specific policies and procedures, including those applicable to its various conservation programs. The principal changes adopted by the Conservancy in the past year are summarized in this memorandum. These changes are intended to achieve the following goals: (1) enable the Conservancy’s Board of Governors to provide increased strategic guidance and undertake more active oversight; (2) incorporate many of the governance principles contained in the Sarbanes-Oxley Act; (3) promote tax law compliance by all parties to conservation transactions in which the Conservancy is a participant; (4) address on a comprehensive and consistent basis issues involving actual or potential conflicts of interest; (5) provide more specific rules guiding key conservation programs such as easements, conservation buyer transactions and sales to governments; and (6) ensure high-level advance review of transactions that may present financial, legal, ethical or other reputational risk to the Conservancy as a whole.

(d) if the donor is a related party or a major donor (as defined) with respect to the Conservancy, the appraiser must also certify that he or she is aware of this fact and that it did not influence the appraiser's valuation.

### Additional Tax Compliance Procedures

Consistent with the practices of many tax-exempt organizations, the Conservancy provides general information to third parties with respect to the potential tax consequences of contributions to and conservation transactions with the Conservancy, but it has long had a written procedure prohibiting the providing of legal and tax advice to third parties. The Conservancy is adopting a more comprehensive procedure to promote tax compliance. Among other things, this new procedure places explicit limits on the types of conservation transactions in which the Conservancy will participate. Specifically, the Conservancy will not enter into any *conservation land transaction that provides tax benefits to a third party* unless the transaction enhances, directly or indirectly, the ability of the Conservancy to carry out its conservation mission; *and* the Conservancy determines that the transaction:

(a) is not a "reportable transaction" within the meaning of section 6011 of the U.S. Internal Revenue Code, relating to tax shelters;

(b) has not been structured to enhance the ability of any person to avoid a tax reporting or substantiation obligation under any federal, state or local tax law; and

(c) is substantially similar to the types of transactions previously approved by the Conservancy.

In general, a type of transaction will be approved by the Conservancy only if an independent and qualified tax counsel could reasonably render an opinion that, upon audit by the IRS or other appropriate tax authority, the anticipated tax benefits "should" be upheld by the tax authority or a court, as opposed to opinions that merely say it is "more likely than not" that the tax benefits claimed would be allowed, or that there is a "reasonable basis" for such a claim.

### **Conflicts of Interest**

The Conservancy has for many years had a formal conflicts of interest policy intended to ensure proper advance review of transactions involving employees, members of the Board of Governors, state chapter trustees and other related parties. This policy has been administered by the Conservancy's Legal Department and the review process has focused primarily on the potential misuse of proprietary or inside knowledge and on whether the terms of all such transactions meet the arm's length standards of applicable law.

The Conservancy has strengthened its conflicts of interest policies in several key areas. First, *purchases and sales of land (including interests in land, such as easements) involving related parties have been prohibited* even though they are permitted under applicable tax laws if structured in accordance with arm's length standards. For this purpose, a "related party" means any person who, within the 12-month period preceding a proposed purchase or sale, was a member of the Board of Governors, a Chapter trustee or an employee. In addition, the prohibition applies to close relatives of any such individual and entities in which the individual and/or a close relative owns more than five percent equity interest.

Second, *other transactions with related parties* (i.e., those that do not involve the purchase and sale of land) will be subject to advance review under the Conservancy's *expanded conflicts procedures*. Under the expanded procedures, a new interdisciplinary committee of experienced Conservancy staff will supplement legal review of all proposed transactions; actual or potential conflicts involving special circumstances (e.g., those with organizational implications and those involving members of the Board of Governors) will be referred to the Audit Committee of the Board for decision; and additional training and guidance will be provided to all employees to enable them to identify potential conflict situations and seek review on a timely basis.

Third, *purchases and sales of conservation lands involving major donors* will be subject to advance scrutiny under the expanded conflicts of interest policy. For this purpose, a "major donor" means any individual, corporation, foundation or other entity that has made gifts or pledges of at least \$100,000 (in cash or in kind) on a cumulative basis within the five-year period preceding the proposed transaction.

Fourth, special rules will apply in the case of *gifts of land (including easements) by related parties and major donors*. In these cases, such gifts will be accepted only if the Conservancy receives a written certification from the appraiser used by the donor to value the land for tax purposes that the appraiser is aware of the relationship between the related party or major donor and the Conservancy and that the relationship did not influence the appraiser's conclusion as to value. In addition, all such gifts would be subject to advance review under the Conservancy's expanded conflicts of interest procedures.

Fifth, while financial supporters of the Conservancy can be elected to the Board of Governors, *if a member of the Board or a company with which he or she is affiliated intends to claim a tax deduction for a gift of land (or an interest in land, such as a conservation easement) to the Conservancy, the transaction will be subject to strict scrutiny by the Conservancy and must be approved by the disinterested members of the Board*. Among other things, this new policy requires *independent assessments by unrelated and qualified persons* of both the conservation value of the land to the Conservancy's mission and of the tax valuations of the gift to be used by the donor.

## Procedures for Specific Conservation Programs

### Conservation Easements

Conservation easements are used in the United States by more than 1,200 organizations and many governmental agencies and have been used by the Conservancy for more than four decades for a broad range of purposes (e.g., providing buffers for core conservation areas, including national parks and other public lands; preserving critical habitats; and conserving watersheds and aquifers to protect aquatic biodiversity and help ensure clean drinking water).

For many years, the Conservancy has had specific procedures governing when conservation easements will be accepted or purchased; requiring preparation of a detailed “baseline” report at the time of acquisition to facilitate future monitoring and enforcement; and mandating the establishment of stewardship funds for finance monitoring and enforcement. In 2001, following consultations with the IRS, the Conservancy established comprehensive procedures governing proposed modifications to easements.

In June 2003, the Conservancy established an Easement Working Group to conduct a comprehensive review of the processes by which the Conservancy acquires, uses, monitors and enforces conservation easements. Based on the Working Group’s recommendations, the Conservancy adopted strengthened procedures requiring, among other things (a) that, consistent with prior practices, prospective donors of easements be informed of the Conservancy’s policies and practices to ensure a clear understanding of mutual expectations and obligations with respect to easements; (b) standardized decision-making on the appropriate location, terms and conditions of easements; and (c) consistent monitoring and enforcement of the terms of the Conservancy’s easements. Proposed modifications to easements have always been subject to advance review by the Legal Department. In addition, proposed modifications involving related parties or major donors now will be subject to advance review and approval under the Conservancy’s strengthened conflicts of interest policies and, as appropriate, by the newly formed Risk Assessment Committee (discussed below).

The Working Group’s final report was presented to and accepted by the Board of Governors in June 2004. At that time, the Board directed the Conservancy’s staff to implement the Working Group’s recommendations through seven specific actions. One of these actions is the establishment of a new centralized easement management electronic database that will include all easements held by the Conservancy and the terms and conditions of each easement. When fully operational, the protocol will (a) notify Conservancy field offices of appropriate monitoring dates for each easement; (b) provide a standardized monitoring checklist; and (c) require that all records of monitoring, property transfer notices, regular owner cultivation, periodic verification of the baseline, and enforcement actions be entered into the system.

### Conservation Buyer Transactions

Conservation buyer transactions typically involve the purchase of land by the Conservancy at its fair market value followed by the sale of the land to an individual or organization (other than a governmental unit or another conservation organization) subject to a conservation easement permanently limiting the uses to which the land may be put. As a result, the restricted value of the land acquired by the conservation buyer is less than the value of the unrestricted land purchased by the Conservancy. In some instances, the Conservancy may seek a contribution from the buyer or a third party to offset its costs, including the cost of acquiring the property.

These transactions permit important conservation objectives to be achieved while the property remains in private hands, on the local tax rolls, and in most cases allowing some compatible economic activity to occur. Of the approximately 10,000 land transactions in which the Conservancy was involved in the last 10 years, 169 were conservation buyer transactions.

As noted previously, conservation buyer transactions may no longer be undertaken with related parties and, in the case of major donors, they may be undertaken only following advance review under the Conservancy's strengthened conflicts of interest procedures. In the case of those conservation buyer transactions that are permitted, additional special policies and procedures are now applicable. Specifically:

(a) to ensure that there is a conservation benefit to the public, the land must fall within a priority conservation site established by Conservancy scientists (which frequently involves consultation with appropriate governmental entities, outside scientists and other knowledgeable sources), and the terms of the easement (and the plan to monitor compliance with those terms) must be structured to achieve the desired conservation result on a permanent basis;

(b) to provide an open and equitable purchase opportunity to all potentially interested parties, the land must be offered for sale in a manner that allows for broad exposure and fair competition among interested buyers;

(c) to ensure that the Conservancy receives fair value for the land, the Conservancy must obtain its own independent appraisal documenting the value of the land both before and after the imposition of the conservation easement;

(d) to ensure compliance with all applicable tax law requirements, if a contribution is solicited in connection with a conservation buyer transaction (i) the Conservancy must document that fact and provide the buyer with a statement of the link between the gift and the sale, and (ii) the transaction must be structured by the Conservancy so as not to relieve the

buyer from substantiating the amount of the contribution for tax purposes;  
and

(e) to ensure that such projects are consistent with local community standards, the Conservancy will obtain community input regarding future uses of the land.

#### Conservation Land Sales to Governments

The Conservancy has for many years had a “no net profit” policy for transfers of land (and interests in land, such as easements) to governmental agencies for conservation purposes. This policy is intended to ensure that the Conservancy only recovers its costs upon such a transfer. Recovery of such costs is also generally limited by the fact that governmental units may only pay fair value for property.

In March 2004, the Conservancy strengthened its “no net profit” policy to provide more specific guidance with respect to inclusion of direct and indirect costs in the Conservancy’s sales prices to governmental entities. In addition, the strengthened policy requires that certain amounts be deducted from the otherwise permissible purchase price. These required reductions include: (1) the value of gifts (including private grants) received and restricted to the conservation lands involved; (2) any government funding received for acquisition or other costs (including costs of capital improvements) relating to the conservation lands involved; and (3) net income received by the Conservancy from any activities (e.g., a significant timber harvest) that have a material effect on the value of the conservation lands involved.

#### Compatible Human Uses

The Conservancy has long recognized that people are an integral part of the landscape and that a reasonable amount of human use of conservation lands must be allowed. To ensure that such uses on property owned by the Conservancy are compatible with basic conservation objectives, the Conservancy has taken the following steps:

(a) to improve its decision-making, the Conservancy will initiate, in cooperation with the United States Fish and Wildlife Service, a review of scientific studies and other literature related to compatible human use;

(b) to improve its understanding of risk and inform future decisions, the Conservancy will conduct a broad survey, based on recommendations of independent scientists, of existing uses of the Conservancy’s preserves; and

(c) innovative, large scale, or untested proposed human uses will be subject to advance review by the Risk Assessment Committee.



In addition, in June 2003, the Board of Governors adopted a policy prohibiting any new oil, gas or hard rock mineral activities on the Conservancy's preserves, except where required by pre-existing contracts or other legal requirements.

### Cause-Related Marketing

The Board of Governors has adopted a policy under which all new uses of the Conservancy's name and logo by third parties must be approved by the Conservancy's President. This responsibility cannot be delegated.

### Legislative Advocacy

To accomplish its conservation mission, the Conservancy often takes a leadership role on ballot funding referenda and other public policy issues. The Board of Governors has clarified that the Conservancy will take positions regarding legislation, rule-making, adjudicatory and other policy matters only if (a) there is a substantial and direct impact on the Conservancy's ability to accomplish its mission, and (b) the Conservancy's position is essential to achieve the desired outcome of the matter in question.

To ensure continued compliance with the tax law requirement that "no substantial part" of its activities consist of attempts to influence legislation, etc., the Conservancy, the Board of Governors has approved an expenditure cap of up to two percent of the Conservancy's budget for such activities. In addition, the Conservancy has provided increased training to its staff.

### **Risk Assessment Committee**

As the preceding discussion illustrates, the Conservancy has a broad range of policies and procedures and many of these have been strengthened over the past year. No set of policies and procedures can identify in advance all possible instances that may present financial, legal, ethical or reputational risks to an organization such as the Conservancy as a whole. Moreover, there are many instances where established policies and procedures would, if literally applied, prohibit the accomplishment of important conservation goals and it therefore may be appropriate in certain specific situations to permit those goals to be accomplished in an alternative manner consistent with the intent and purposes of the applicable policies and procedures.

To address these issues, the Conservancy has created a Risk Assessment Committee whose activities are modeled on the committee review process increasingly used by decentralized firms, in the financial services sector and elsewhere, for risk review. The committee conducts advance reviews of those projects, transactions, and issues that meet its criteria for review (e.g., transactions that are new, novel or particularly complex, and transactions that comply with applicable legal and tax requirements and Conservancy policies, but nevertheless involve potentially substantial financial, ethical or reputational risk to the Conservancy). Particular attention is given to ensuring consistency of projects with the Conservancy's stated values.

The committee's members consist of experienced Conservancy personnel representing all relevant disciplines necessary to evaluate critically the organizational risks associated with the types of projects, transactions, and issues to be reviewed. The committee endeavors to promote intelligent and prudent entrepreneurship by helping innovative conservation projects succeed wherever feasible. Thus, the committee has the ability not simply to approve or disapprove a proposed project or transaction, but to grant approval conditioned on restructuring the project or transaction in ways that will address organizational risks effectively and ensure full compliance with all applicable laws and relevant ethical considerations.

# Strengthened Governance

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## **Summary of Actions Taken to Strengthen Governance, Policies and Procedures June 2003 – March 15, 2005**

Over the past 22 months, The Nature Conservancy conducted a comprehensive, top-to-bottom review of its practices with the assistance of an expert and independent advisory panel. The panel presented a set of far-reaching recommendations for strengthening organizational oversight. The Conservancy has adopted virtually all of the panel's recommendations, and made numerous additional changes that affect nearly every aspect of the Conservancy's day-to-day operations. All told, the Conservancy has made dozens of changes to ensure it is acting in accordance with the highest standards. Highlights of these changes follow.

### Strengthening Governance Roles and Responsibilities

The Board of Governors increased its day-to-day organizational oversight of the Conservancy by creating a more active Executive Committee (now meets a minimum of seven times a year) and restructuring its other committees. Board members serve on only one committee so that they can focus their time and be more deeply involved in oversight and management. The Conservancy also created a new management and Board structure that enhances the Board's ability to carefully and thoroughly assess and manage organizational and reputational risks.

In the past, the Conservancy's decentralized structure made it difficult to oversee the conservation decisions of the organization's various chapters. Now, a new trustee council is helping bridge the span between central and local operations with new written standards and comprehensive operating principles for all 1,500+ trustees serving on more than 50 chapter boards.

### Sarbanes-Oxley Reforms

While not required for nonprofits, the Conservancy has adopted many of the core principles of the Sarbanes-Oxley Act of 2002. Its financial statements are audited, with auditors selected by the Board's Audit Committee, and the lead audit partner is rotated every five years. Internal audit staff's investigative role has been expanded, and additional procedures are in place to ensure internal audit findings are acted upon and compliance is documented. The Conservancy has created and filled the position of chief compliance officer. This person is responsible for ongoing training of all staff and establishing systems to promote compliance with all applicable laws, the Conservancy's policies and procedures, and the highest ethical standards. All key managers attend training and execute an annual certification saying that they and their staff have complied with the Conservancy's policies and procedures and certifying that any conflicts have been disclosed. A whistleblower policy and hotline are in place to protect employees who wish to report a potential violation. The Board determines executive compensation, and no loans can be made to directors, officers or employees. The Conservancy has also taken important steps to improve the transparency and public understanding of its Form 990 filings. The Conservancy's Form 990 for Fiscal Year 2003 included more information about the Conservancy's governance and its direct charitable programs and accomplishments.

### Addressing Potential Conflicts of Interest

The Conservancy's long standing conflicts of interest policy has been strengthened in several respects that go well beyond legal requirements, including an expanded definition of who is considered a related party. The Conservancy considers Board members, trustees, staff and their immediate families and major donors to be related parties. This expanded definition not only increases the number of potential conflicts that require advance review and approval, but also ensures that actual, as well as perceived, conflicts of interest are disclosed, reviewed, and properly handled. The process for reviewing conflicts has also been expanded

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beyond the General Counsel's office to involve review by a high-ranking staff Conflicts Committee. Cases involving Board members and major donors require review and approval from the Board's Audit Committee. New training programs have been implemented to help staff spot and properly address cases that involve even the appearance of a conflict.

In addition, some transactions – although allowed by law – have been prohibited completely to avoid even the appearance of impropriety (e.g. purchases and sales of land, including conservation easements, involving related parties such as Board members, trustees, employees, and the families of these groups).

#### Strengthening Policies for Specific Conservation Transactions

*Conservation Easements.* The Conservancy accepts conservation easements only on lands that fall within scientifically identified ecologically important priority landscapes. Based on the yearlong efforts of its Conservation Easement Working Group, the Conservancy is strengthening its policies and procedures on the documentation, monitoring, and enforcement of easements. In 2001, following consultations with the IRS, the Conservancy established comprehensive procedures governing proposed modifications to easements. These procedures were strengthened in 2003 as part of the Conservation Easement Working Group changes. The Conservancy will not agree to a substantive modification of an easement unless the original conservation purpose of the easement is not compromised, the General Counsel's office determines that the modification does not result in a net private economic benefit, and approval is granted from the relevant state authority. To promote tax law compliance by donors, the Conservancy will not sign IRS Form 8283 certifying receipt of a land contribution, such as an easement, unless the Conservancy receives a copy of the appraisal to be used by the donor in establishing tax values, and a written certification by the appraiser that IRS "qualified appraisal" standards have been followed. Additionally, in situations involving donations from Board of Governors members, trustees, staff, the immediate family of those three groups, and major donors the appraiser must also certify that the relationship did not influence his or her appraisal. (Existing tax law requires only that the Conservancy certify receipt of the gift.)

*Land Sales to Governments.* The Conservancy's long-standing "no net profit" policy is designed to ensure that the organization recovers only its costs, even if the land has increased in value while held by the Conservancy. The organization strengthened this policy to better account for the direct and indirect costs associated with acquiring, holding, and managing land pending a sale to the government. The policy also was strengthened to ensure that the value of a land gift, any government funding related to the acquisition of that property, and any other significant income derived from the property are passed on to the government.

*Conservation Buyer Transactions.* Conservation buyer transactions are designed to keep conservation lands in private hands. In these transactions, the Conservancy acquires a piece of property and sells it to a private buyer subject to a conservation easement designed to permanently preserve the land's ecological values. The easement reduces the value of the land and the Conservancy sells the property for its new fair market value reflective of the easement encumbrance. All of the Conservancy's conservation buyer transactions served important conservation purposes and complied with all applicable laws. Of the 10,000 Conservancy land transactions conducted over the past 10 years, less than two percent, or 169, were conservation buyer transactions. Of those 169, only 19 were with trustees or employees of The Nature Conservancy. All of these properties were sold for fair market value and subjected to conflicts of interest review. Nevertheless, the Conservancy no longer engages in conservation buyer transactions with related parties. All conservation buyer properties must be in a priority site as identified by Conservancy scientists. The organization now widely advertises each property to provide a fair purchase opportunity to all, relies on independent appraisals to ensure it receives fair market value, and follows specific procedures to make transactions more transparent and to promote appropriate tax treatment.

TNC Proposals for Legislative Changes  
to Improve Conservation Transactions

This memorandum outlines a series of possible changes that The Nature Conservancy supports that would be made to the Internal Revenue Code to strengthen existing law and regulations to improve conservation transactions. These proposals seek 1) to ensure that the valuations of land and interests in land, such as conservation easements, that are used for federal tax purposes are established in accordance with the highest professional standards and are proper; 2) to ensure that a significant conservation benefit to the public will be achieved in conservation transactions; and 3) to ensure that there is compliance with the terms and restrictions in conservation easements and that the organizations and entities that hold conservation easements fulfill their obligations to monitor and enforce such interests in land. The Conservancy also supports new incentives that are needed to help private landowners who wish to voluntarily protect their land.

Tax Valuations<sup>1</sup>

1. Require Second Appraisal for Certain Contributions. Contributions of property described in section 170(h) for which a tax deduction is otherwise allowable under section 170(a) must be supported by a “qualified appraisal” as defined in Treas. Regs. 1.170A-(c)(3). A second qualified appraisal could be required for certain large contributions (e.g., where the value of the property exceeds a certain dollar threshold including the value of similar contributions within the preceding five years) and for property involving a potential for self-dealing (e.g., subject to a *de minimis* rule for small gifts, contributions to a nongovernmental donee organization where the donor would be a disqualified person under section 4946 if the donee organization were a private foundation as defined in section 509(a)). Under this special two appraisal rule, the donor could not claim a deduction in excess of the average of the two appraisals. To prevent abuse, the deduction could in no event exceed a specified percentage (e.g., 125 percent) of the lowest appraisal. Donors subject to the two appraisal rule could be required to identify the contribution transactions on their tax returns in the same manner as transfers to foreign trusts are now required to be reported. They also could be required to disclose any additional appraisals obtained in connection with the contribution. Finally, in order to provide an incentive to landowners to obtain such appraisals, a ‘safe harbor’ would be provided such that the deduction claimed would be presumed to be valid where the donor complied with the rules and procedures in this area.

2. Codify the Offsetting Increase in Value Rule. The current rule contained in the easement regulations requiring qualified appraisals to take into account any increases in value resulting from the contribution for which a tax deduction is claimed could be codified and expanded to include all gifts of land (not just easements) provided that such

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<sup>1</sup> The valuation and penalty proposals could also be applied to all gifts (including bargain purchases) of land for conservation purposes (as described in section 170(h)(4) of the Code).

land contributed was to be devoted to an open space or conservation land use. This would ensure that the requirement would be applied in all cases and that the effects on the value of other property owned by the donor (e.g., cases involving land adjacent to residential developments that incorporate greenways and other open spaces) would be taken into account whenever appropriate.

3. Improve Appraiser Qualifications and Appraisal Methods. The person making the qualified appraisal could be required to certify under penalties of perjury that (a) he/she is a State General Certified appraiser, as those terms are defined by the Appraiser Qualifications Board under authority of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989; (b) in making the appraisal, the appraiser applied generally accepted appraisal standards which would be interpreted to mean conformance with the Uniform Standards of Professional Appraisal Practice (USPAP) standards; and (c) the appraiser has not been barred from presenting evidence or testimony in any administrative proceeding before the Department of the Treasury or the Internal Revenue Service.

4. Increase Penalties for Improper Valuations of Conservation Easements. Section 6662 could be amended to provide increased penalties with respect to the valuation of conservation easements and section 6700 could be amended to extend the penalties provided therein to persons who make or furnish appraisals of conservation easements.

#### Assuring Conservation Purposes and Public Benefits

5. Public Disclosure of Conservation Easements, Purpose and Modifications. Each nongovernmental donee organization could be required to prepare annually a list of all easements it has received as a donation and for which tax benefits had been claimed setting forth the location of the property; the acreage of the property; the conservation purpose of the easement; and whether there has been any modification to the easement (and, if so, the terms of the modification). This list would be required to be filed with the donee organization's Form 990 and made available for public inspection in the same manner as other portions of the organization's Form 990 are made available.

6. Prohibit Easement Deductions for Specific Transactions. Specific conservation transactions that would by definition lack any significant conservation purpose or public benefit should be identified and specifically excluded from being eligible for the tax benefits provided to encourage legitimate conservation transactions. Such transactions might include easements over golf courses for example. Explicit criteria could also be included in legislation to identify the specific types of projects that would be ineligible for favorable tax treatment. Procedures could be established for the IRS to consider exceptions for approval on a case by case basis, if specified conservation purpose criteria were met.

7. Accreditation. The Secretary of the Treasury could be authorized, but not required, to select a private, nonprofit entity with appropriate expertise and experience to

form an accrediting body to establish a voluntary accreditation system to evaluate and accredit the competence of qualified organizations to manage donations of qualified conservation easements. Any donee organization that voluntarily sought and was accredited would be deemed to have met the statutory requirements for reasonable conservation easement monitoring and enforcement procedures and adequate resources for same.

#### Easement Compliance, Monitoring and Enforcement

7. Limitations on Modifications to Easements. Deductions for a grant of a conservation easement to a nongovernmental donee could be disallowed unless the terms of the easement provide that no amendment to the conservation terms of the easement (including any amendment reducing the acreage subject to the easement) may be made having the effect of reducing the overall level of conservation purposes sought to be achieved under the original easement unless the donor (or his/her successor in interest) and the donee organization secure the advance written approval of the relevant State authority that provides oversight of charitable organizations within the State where the property is located (or, if there is no such authority, a court of competent jurisdiction within that State). The donor (or his/her successor in interest, if applicable) would be required to report any such modification on his/her tax return for the year in which the modification occurred.

8. Monitoring of Compliance with Easements. Each nongovernmental donee organization could be required to certify annually on its Form 990 that it has established and implemented reasonable written procedures for monitoring compliance with the terms of the conservation easements it receives and that (as now required by regulations) it has adequate resources to enforce those restrictions. No single set of specific monitoring procedures would be established for all donees. The legislative history could make clear that this requirement would be met if, for example, a donee organization required each owner of property subject to an easement in the donee's favor annually to certify to the donee that the terms of the easement had not been violated and if the donee had a program in place to verify such certifications on a "test check" basis. As in the case of procedures used by private foundations in making grants to individuals, a donee organization could obtain a ruling from the Internal Revenue Service that its procedures were reasonable.

9. Violations of Terms of Easements. The tax benefits attributable to a prior donation of a conservation easement could be recaptured, with interest, if the terms of the easement are violated intentionally by the donor or a related person. (This proposal has been included in President Bush's Administration current Budget proposal.) Provisions would need to be included to ensure that procedures were in place to allow such violations to be cured. Until the property burdened by the easement had been transferred to an unrelated party, the donor could be required annually to certify on Form 1040 that there has been no violation (caused by the donor or related person) of the conservation terms of a previously donated easement.

10. Additional Resources Provided to the IRS. In order to ensure effective enforcement of the conservation easement rules and valuation procedures, additional resources must be provided to the IRS to conduct its audit and enforcement activities in this area. It would be appropriate to levy modest fees based on the annual tax benefits to be claimed and realized by the donor to create a pool of funds to support IRS activities in this area. In addition, any over-valuation penalties levied against improper valuations claimed by taxpayers or their advisors should also be allocated to this fund.

Additional Incentives for Private Landowners to Encourage Conservation Activities

TNC strongly supports passage of additional incentives for private landowners who voluntarily choose to protect their land for conservation purposes. Such incentives have been sponsored by Senators Grassley and Baucus and are included in the current version of the CARE bill (S. 6, introduced by Senator Santorum in the 109<sup>th</sup> Congress) . These incentives are needed to ease the financial burden and to enhance the net after tax return to the typical ‘land-rich, cash poor’ private landowner for whom the current set of incentives is not meaningful. These incentives would reduce the capital gains tax on sales of land or interests in land for conservation purposes and would enable the landowner who makes a living from the land to use all of the available tax benefits from a gift of an easement against their income. President Bush included the proposal to reduce the capital gains tax on sales of land or interests in land for conservation in the Administration’s current Budget proposal, as he has done since he was elected President.



## Overview of Reforms at The Nature Conservancy

Based on recommendations from an internal top-to-bottom review, a Board of Governors' Audit Committee review of the Sarbanes-Oxley Act, and the recommendations of a Board-chartered panel of outside experts, The Nature Conservancy initiated a series of organization-wide changes to strengthen its governance practices and oversight; improve risk assessment and management; increase transparency and accountability; clarify potential conflicts of interest; enhance the roles of trustees; and implement key Sarbanes-Oxley principles. Below is a brief overview of the extent and nature of these organizational changes.

March 15, 2005

	Previous Practice	Current Practice/Changes
<b>Governance &amp; Oversight</b>	<ul style="list-style-type: none"> <li>▪ <i>Composition:</i> A Board of Governors was chartered for 41 members that met at least three times each year.</li> <li>▪ <i>Committees:</i> Six committees each led by two co-chairs; members served on multiple committees.</li> <li>▪ <i>Executive Committee:</i> Executive Committee chartered but was not active.</li> </ul>	<ul style="list-style-type: none"> <li>▪ <i>Composition:</i> The Board of Governor's size and frequency of meetings has remained the same.</li> <li>▪ <i>Committees:</i> Restructured each of the six committees based on comprehensive and formal charters to provide strategic guidance; conduct active oversight; including executive compensation; and define and manage relationships with chapters. Board members serve on only one committee so that they can focus their time and be more deeply involved in oversight and management. Entire Board is required to meet in person three times a year, and often additionally meets by telephone conference.</li> <li>▪ <i>Executive Committee:</i> The Executive Committee is comprised of the chairmen of the six committees, the Chairman, Vice Chairman, and Secretary of the Board of Governors. In addition to the regularly scheduled thrice-yearly Board meetings, the Executive Committee also meets a minimum of four times a year.</li> </ul>

	Previous Practice	Current Practice/Changes
<b>Sarbanes-Oxley Reforms</b>	<ul style="list-style-type: none"> <li>▪ The Sarbanes-Oxley law does not pertain to charities and was only enacted a few years ago.</li> <li>▪ In 2002, the Audit Committee commissioned a Sarbanes-Oxley review to determine applicability of the principles to charitable organizations.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Several Sarbanes-Oxley-related enhancements were implemented, including a “whistleblower” policy; adoption of new policies concerning related parties; prohibiting any loans to directors, officers or staff; increased transparency about the organization and its activities; and a new approach to identifying and assessing potential business risk.</li> <li>▪ Details on the implementation of these and other policies are listed below: <ul style="list-style-type: none"> <li>▪ <i>External Audits:</i> The Conservancy’s external auditor is approved annually by the Board, and the Audit Committee reviews the Conservancy’s contract with its external auditor every five years, the lead audit partner is rotated every five years.</li> <li>▪ <i>Internal Audits:</i> Under the supervision of the Audit Committee of the Board, the scope of internal audits was expanded and internal auditors are authorized to perform internal investigatory functions similar to those performed by Inspectors General in federal governmental agencies. There are procedures to ensure internal audit findings are acted upon. Procedures, including focused training for senior managers, have been implemented to identify and take appropriate remedial actions with respect to internal audit findings that have system-wide implications.</li> <li>▪ <i>Compliance Documentation:</i> Requirement that all key managers attend training and execute an annual certification that they and their staff have complied with the Conservancy’s policies and procedures and certifying that any conflicts of interest have been disclosed.</li> <li>▪ <i>Whistleblower policy:</i> Adoption of a “whistleblower” policy and procedure to ensure that any employee who wishes to report a potential violation of law, policy or procedure may do so without fear of retaliation.</li> <li>▪ <i>Chief Compliance Officer:</i> Creation of a new senior-level position responsible for establishing systems to promote training and compliance with all applicable laws, the Conservancy’s policy and procedures, and the highest ethical standards.</li> <li>▪ <i>Increased Transparency:</i> The Conservancy’s IRS Form 990 for fiscal year 2003 has been expanded to include more information about the Conservancy’s governance and its direct charitable programs and accomplishments. This and past 990 Forms are available on the Conservancy’s Web site.</li> </ul> </li> </ul>

	Previous Practice	Current Practice/Changes
<b>Assessing &amp; Managing Risk</b>	<ul style="list-style-type: none"> <li>▪ <i>Risk Assessment:</i> The Board of Governors reviewed only land acquisition transactions in excess of \$2 million.</li> <li>▪ <i>Managing Risk:</i> The Board focused on financial risks posed by the Conservancy's land acquisition work.</li> </ul>	<ul style="list-style-type: none"> <li>▪ <i>Risk Assessment and Management:</i> The Projects and Activities Review Committee of the Board assesses a wide variety of projects, transactions, and issues that meet its criteria for review (e.g. transactions that are new, novel or particularly complex, or involve potentially substantial financial, ethical or reputational risks to the Conservancy).</li> <li>▪ The Board created a staff Risk Assessment Committee to supplement the Board's review process. The staff committee reports directly and regularly to the Projects and Activities Review Committee.</li> <li>▪ All land acquisition transactions in excess of \$2 million still require review by the Board of Governors.</li> </ul>
<b>Conflicts of Interest</b>	<ul style="list-style-type: none"> <li>▪ <i>Policy:</i> A formal conflicts of interest policy intended to ensure any transaction involving a related party was handled appropriately, including ensuring advance review of transactions involving employees, members of the Board, and state chapter trustees.</li> <li>▪ <i>Review:</i> Potential conflicts reviewed by General Counsel.</li> <li>▪ No mandatory prohibitions on transactions with related parties.</li> </ul>	<ul style="list-style-type: none"> <li>▪ <i>Policy:</i> Expanded definition of "related parties" to include major donors and the immediate families of Board of Governor members, trustees, and staff.</li> <li>▪ <i>Review:</i> Formation of a multi-disciplinary Staff Conflicts of Interest Committee to supplement legal review.</li> <li>▪ Sales and purchases of land and interests in land to or from Board of Governors members, trustees, staff, and the immediate families of these groups are expressly prohibited.</li> <li>▪ Other transactions with related parties (not purchases or sales of land) are subject to advance review under conflicts procedure.</li> <li>▪ Land and other transactions involving major donors are subject to advance review and approval under conflicts procedure.</li> <li>▪ All conflicts involving Board of Governor members, major donors or other insiders are referred to the Audit Committee of the Board.</li> <li>▪ A Board member or his/her company may not claim a tax deduction for a gift of land unless the transaction is independently reviewed, scrutinized, and approved by Board of Governors.</li> <li>▪ Board of Governors members and their companies cannot engage in cause related marketing agreements with the Conservancy.</li> <li>▪ Training programs have been initiated to enable staff to identify and address cases that involve even the appearance of a conflict.</li> </ul>

	Previous Practice	Current Practice/Changes
<b>Promoting Tax Compliance</b>	<ul style="list-style-type: none"> <li>▪ In compliance with IRS regulations, the Conservancy would certify that it received a gift by signing an IRS Form 8283. In signing the form, the Conservancy was only acknowledging receipt of the gift, not agreeing with or having knowledge of the donor's valuation of the gift or the deduction claimed.</li> </ul>	<ul style="list-style-type: none"> <li>▪ 8283 Review: Created stricter policies above and beyond IRS requirements for executing Form 8283, including a requirement that all required information be filled out, that the Conservancy receive a copy of the appraisal to be used by the donor to substantiate the value of a donation, and a written certification by the appraiser that the IRS "qualified appraisal" standards have been followed.</li> <li>▪ The Conservancy will not participate in transactions in which the appearance of the transaction is suspect or unreasonable, or where the transaction does not conform to the 8283 policy.</li> <li>▪ If the donor is a Board member, trustee, staff or immediate family of those groups, or a major donor, the certification must include a statement that the appraiser is aware of the donor's relationship to the Conservancy and that the relationship did not influence the appraisal.</li> </ul>

	Previous Practice	Current Practice/Changes
<b>Conservation Easements</b>	<ul style="list-style-type: none"> <li>Conservancy had specific procedures governing when conservation easements will be accepted or purchased; requiring preparation of a detailed "baseline" report at the time of acquisition to facilitate future monitoring and enforcement; and mandating the establishment of stewardship funds to finance monitoring and enforcement.</li> <li>In 2001, following consultations with the IRS, the Conservancy established comprehensive procedures governing proposed modifications to easements.</li> </ul>	<ul style="list-style-type: none"> <li>Donations of conservation easements by related parties including major donors are still permitted, subject to advance review and approval under strengthened conflicts of interest procedures.</li> <li>The Conservancy adopted new policies and procedures for the way the Conservancy acquires, documents, monitors, and enforces conservation easements, including: <ul style="list-style-type: none"> <li>Standardized decision-making on location, terms and conditions of easements.</li> <li>Stricter set of standards for approving easement modifications involving related parties.</li> <li>Consistent monitoring and enforcement of the terms of Conservancy easements to ensure that conservation goals are met and easement terms are enforced. Now as part of routine audits, the Conservancy's internal audit staff checks to see if easements are being monitored and that monitoring site reports are being filed.</li> <li>Particularly large, risky or potentially controversial easement donations will be referred to the Risk Committee.</li> <li>The Conservancy will inform prospective donors of the terms and conditions for acceptance of easements to ensure a clear understanding of mutual expectations and obligations.</li> </ul> </li> <li>The Conservancy ensured that the organization was prepared to implement new procedures by taking actions such as establishing a new centralized database that lists all easements, and once fully operations will notify Conservancy field staff when a specific easement should be monitored, and provide a standardized monitoring checklist.</li> </ul>
<b>Conservation Land Sales to Governments</b>	<ul style="list-style-type: none"> <li>Long standing "no net profit" policy.</li> </ul>	<ul style="list-style-type: none"> <li>Although the Conservancy has a long standing (1995) policy of recovering only its costs when transferring real estate to a government agency, additional procedures were implemented to better define allowable costs and to ensure that the value of gifts received and restricted to the property, any prior government funding related to that property, and any other significant net income derived from the property are passed on to the government entity.</li> </ul>

	Previous Practice	Current Practice/Changes
<b>Conservation Buyer Transactions</b>	<ul style="list-style-type: none"> <li>▪ Less than 2% of land transactions in the last 10 years were conservation buyer transactions (169 of 10,000) Only 19 of the 169 were with Conservancy staff or trustees.</li> <li>▪ All transactions served important conservation goals and complied with all applicable laws.</li> </ul>	<ul style="list-style-type: none"> <li>▪ In addition to the prohibition of land purchases from or sales to Board of Governors members, trustees, staff and their families, the Conservancy created five new procedures providing that: <ul style="list-style-type: none"> <li>▪ Land must be in a priority site as identified by Conservancy scientists;</li> <li>▪ Property must be publicly marketed;</li> <li>▪ Conservancy must obtain independent appraisal for property before and after easement;</li> <li>▪ Specific rules are implemented to make transactions more transparent to ensure appropriate tax treatment; and</li> <li>▪ Conservancy will obtain community input about future uses of land.</li> </ul> </li> </ul>
<b>Compatible Human Uses</b>		<ul style="list-style-type: none"> <li>▪ Prohibition on any new oil, gas or hard rock mineral activities on Conservancy preserves, except where required by law.</li> <li>▪ Board determined that human-use can occur on Conservancy preserves in four circumstances. Untested, innovative or large-scale human uses must be reviewed by Risk Assessment Committee.</li> <li>▪ Conservancy initiated review of scientific literature and a survey about existing human use on the Conservancy's land.</li> </ul>
<b>Cause Related Marketing</b>	<ul style="list-style-type: none"> <li>▪ The Conservancy followed the cause-related guidelines recommended by the Better Business Bureau's Wise Giving Alliance in its "Standards for Charitable Accountability."</li> <li>▪ Cause related marketing agreements approved by the Vice-President of Marketing and Philanthropy.</li> </ul>	<ul style="list-style-type: none"> <li>▪ All new uses of the Conservancy's name and logo by third parties must be approved by the Conservancy's President.</li> <li>▪ The Board of Governors reviews cause related marketing agreements annually and must approve all agreements with companies whose businesses, products or services may appear in conflict with the Conservancy's mission.</li> <li>▪ The Conservancy will not enter into a cause related marketing agreement with a Board of Governor member or his/her company.</li> </ul>
<b>Related Organizations</b>	<ul style="list-style-type: none"> <li>▪ General Counsel and Director of Finance could approve the formation of a related entity if the financial commitment for the entity was under \$2 million.</li> <li>▪ Board of Governors approval was required for the formation and operation of any related organizations which would exceed a financial commitment of \$2 million.</li> </ul>	<ul style="list-style-type: none"> <li>▪ The Conservancy adopted a policy requiring Board approval for the formation and operation of any related organizations to ensure that the related entities are consistent with the Conservancy's goals and objectives and that related risks are identified and appropriately managed.</li> <li>▪ Related entities where the Conservancy has a significant business interest (investment of \$100,000+), but not a controlling interest must be approved by the President.</li> </ul>

	Previous Practice	Current Practice/Changes
<b>Roles of Trustees</b>	<ul style="list-style-type: none"> <li>▪ <i>Role of Trustees:</i> A document outlining the role of trustees was developed, but it was not well understood.</li> <li>▪ <i>Responsibilities:</i> Each of the more than 50 chapter boards had its own by-laws and standards of governance.</li> </ul>	<ul style="list-style-type: none"> <li>▪ <i>Role of Trustees:</i> Four consistent roles have been identified for chapter board of trustee members: Ambassador, Conservationist, Fundraiser, and Advisor.</li> <li>▪ <i>Responsibilities:</i> Developed an effective system of minimum standards for chapter boards and individual trustees as well as a set of best practices to be administered consistently across the organization.</li> <li>▪ <i>Trustee Advisory Council:</i> Provides input to Board of Governors on major policy decisions and organizational initiatives.</li> </ul>